

## Filling the infrastructure investment gap.

The role of Project Preparation Facilities:  
an overview of MDBs and the  
Inter-American Development Bank  
approach

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Vice Presidency for Countries

DISCUSSION  
PAPER N°  
(IDB-DP-00603)

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Reinaldo Fioravanti, Carolina Lembo and Akash Deep



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# 1. Introduction

The Inter-American Development Bank (IDB) is working with other multilateral development banks (MDBs) and international organizations (IOs) to define common mechanisms and policies to tackle the infrastructure gap in Latin America and the Caribbean (LAC) by attracting more private investment, among other measures and initiatives.

Governments, MDBs and IOs currently agree that private investment will flourish in a more favorable environment, one in which the political, institutional and regulatory context attract private investment. An additional challenge for securing private investment in infrastructure is a general lack of well-prepared projects that are attractive to private partners.

Large infrastructure projects require a great deal of planning in the pre-investment phase, including studies that address the technical, environmental, social, financial and legal challenges associated with a project. When executed properly, such studies can reveal unanticipated insights, enabling both public and private parties to mitigate and price those newly identified risks.

This paper provides reflections and considerations as to how MDBs including the IDB can use the Project Preparation Facilities (PPFs) to help countries fill the infrastructure gap by improving the quality of projects, reducing and mitigating risks, and leveraging private financing.

Similar studies have been conducted for PPFs in Asia<sup>1</sup>, Africa<sup>2</sup> and Europe<sup>3</sup>. However, there is no similar assessment for LAC. This paper is the first step towards utilizing the resources offered by PPFs for infrastructure development projects in LAC, and applying these useful tools to another critical region.

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<sup>1</sup> G20 Development Working Group. *Assessment of the Effectiveness of Project Preparation Facilities in Asia*. Adam Smith International, September 2014.

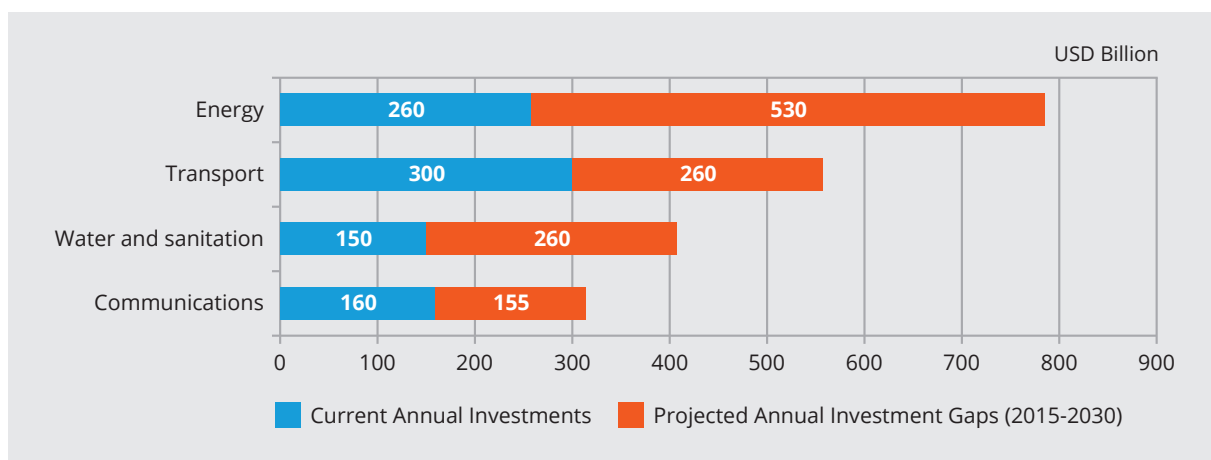
<sup>2</sup> World Economic Forum. *Africa Strategic Infrastructure Initiative: a principled approach to Infrastructure Project Preparation Facilities*, In collaboration with The Boston Consulting Group, June 2015.

<sup>3</sup> European Bank for Reconstruction and Development. *Proposal for an EBRD Infrastructure Project Preparation Facility*. 2015.

## 1.1. The Infrastructure Gap and the MDB roles

Infrastructure is crucial for generating economic and social development and reducing inequality.<sup>4</sup> The current gap<sup>5</sup> in global infrastructure investment impedes sustainable economic growth and trade, suppresses job creation and hinders efforts for inclusive development. In 2014, infrastructure financing in developing countries was estimated at around 1 trillion USD per year. This is less than the projected infrastructure investment need for the period of 2015-2030: 1.2 trillion USD. (Figure 1).<sup>6</sup>

Figure 1 – Infrastructure Financing in Developing Countries and Projected Investment Gaps



Source: OCDE 2015

To close the infrastructure gap, the LAC region should invest at least 5% of GDP in infrastructure for an extended period (Figure 2). In absolute terms this would be approximately 250 billion dollars. In the 1990s, investment in infrastructure in LAC fluctuated between 2% and 3% of GDP, placing the region short of its required investment goal, equivalent to an annual shortfall of around 100-150 billion USD.<sup>7</sup>

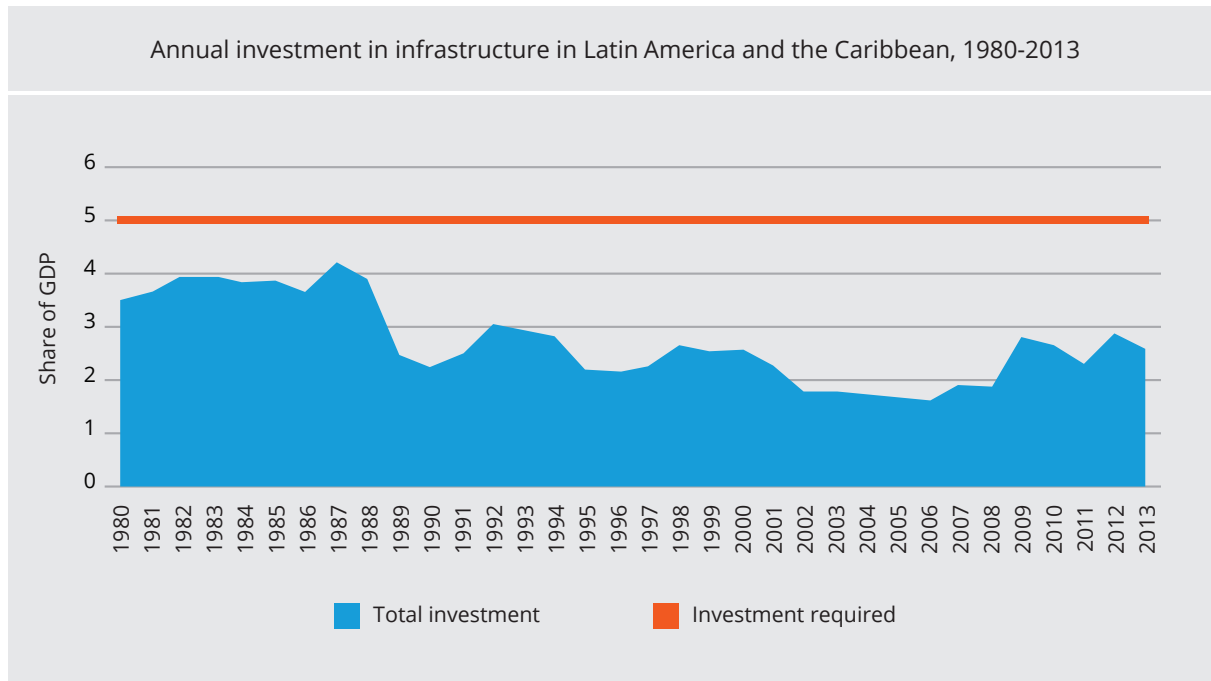
<sup>4</sup> Cesar Queiroz; Gaston Astesiano y Tomas Serebrisky. An overview of the Brazilian PPP experience from a Stakeholders' viewpoint. Inter-American Development Bank, Technical Note No. IDB-TN-641, 2014, p. 10.

<sup>5</sup> Usually the infrastructure gap is measured by the infrastructure needed to: "(a) meet a target of Gross Domestic Product (b) achieve a specific objective, such as a coverage rate (for example, 100 percent access to water and sanitation), or (c) achieve an infrastructure stock similar to a country or group of countries". Tomás Serebrisky et al. *Financing Infrastructure in Latin America and the Caribbean: How, How Much and by Whom?* Inter-American Development Bank, 2015, page 8.

<sup>6</sup> OECD. Official Development Finance for Infrastructure support by Multilateral and Bilateral Development Partners. OECD report to G20 Finance Ministers and Central Bank Governors, September 2015, page 9.

<sup>7</sup> Tomás Serebrisky et al. *Financing Infrastructure in Latin America and the Caribbean: How, How Much and by Whom?* Inter-American Development Bank, 2015, page 16.

Figure 2 – Annual investment in infrastructure in Latin America and the Caribbean, 1980-2013



Source: IDB, 2015.

The decline in infrastructure investment was due to reductions in public investment as a whole, which amounted to only 1% of GDP during the 1990s. This level of investment did not change significantly until 2006, thanks to prudent macroeconomic policies implemented in the region which increased fiscal space. The LAC has a history of private investment in infrastructure projects sporadically throughout the 20<sup>th</sup> century, but there is still heavy reliance on public investment, as in other regions of the world<sup>8</sup>.

Governments and MDBs agree that private sector participation is critical for closing the infrastructure gap<sup>9</sup> in the coming years. Engaging the private sector offers not only a new source of financing but also the efficiency and culture of private organizations (i.e. new technologies; different organizational solutions)<sup>10</sup>.

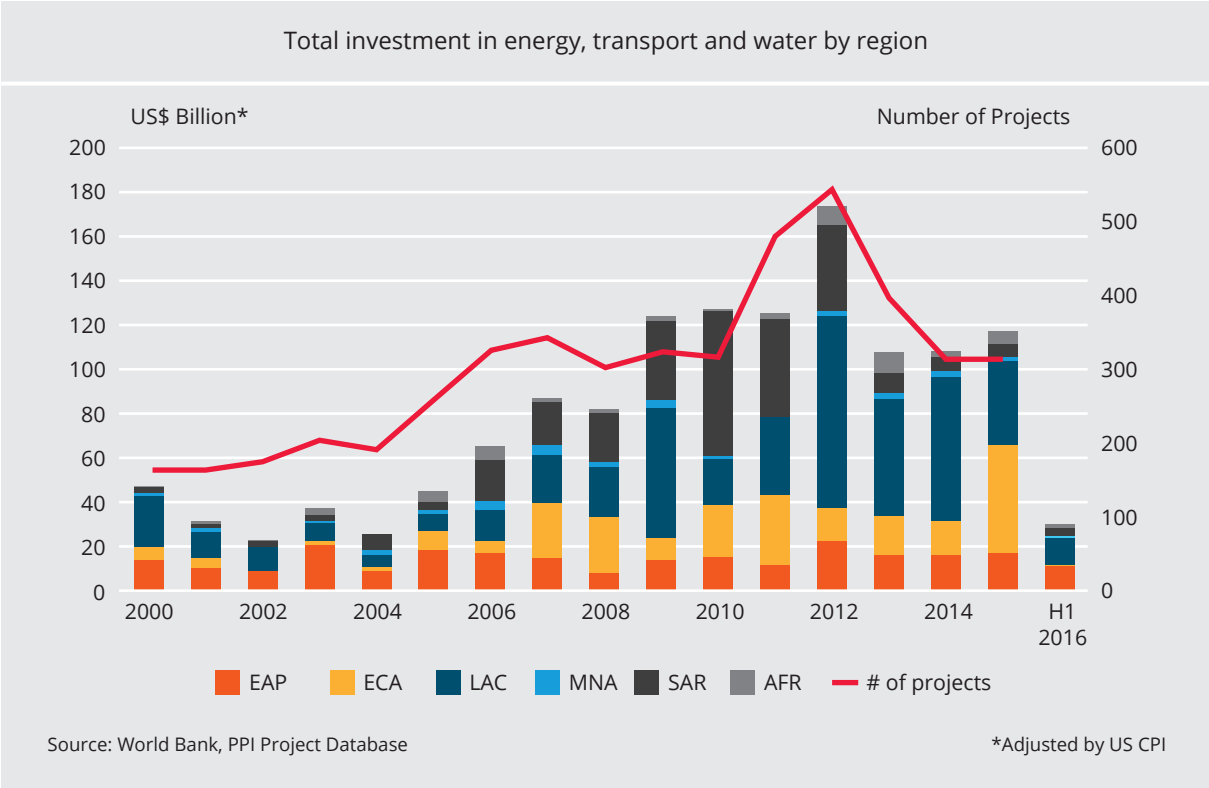
<sup>8</sup> Banco Interamericano de Desarrollo. *Ahorrar para Desarrollarse: Cómo América Latina y el Caribe puede ahorrar más y mejor*, 2016. Disponible en: <http://www.iadb.org/es/investigacion-y-datos/ahorrar-para-desarrollarse-como-america-latina-y-el-caribe-pueden-ahorrar-mas-y-mejor,19956.html>

<sup>9</sup> “Currently, the additional infrastructure investment needed in the developing world to meet the 2030 agenda for sustainable development is estimated to be \$1 trillion to \$1.5 trillion annually over the next 15 years. This is a capital requirement that cannot be met by public sources of finance alone. While the MDBs represent only a small percentage of the financing for infrastructure, they play a critical role in improving upstream activities such as legal and institutional frameworks strengthening, readiness of the PPP environment, project preparation and structure in order to attract private capital”. G20 Meeting. MDBs’ Joint Declaration of Aspirations on actions to support infrastructure investment, 2016, page. 1.

<sup>10</sup> Asian Development Bank. Public-Private Partnership Operational Plan 2012-2020., 2012, page 6.

Private participation in infrastructure in developing countries has never exceeded 1/3 of total infrastructure funding<sup>11</sup>. In 2016, the percentage for the first quarter was slightly higher as compared to 2015 in global numbers and in LAC has shown approximately 40%. (Figure 3)

Figure 3 – Total Private Sector Investment in Energy, Transport and Water by Region



One of the advantages of well-designed Public Private Partnerships (PPPs)<sup>12</sup> is that they bring private financing to public infrastructure projects, thereby expanding the fiscal space available to governments. Bridging the so-called “financing gap” has therefore been the primary intervention used by national banks, MDBs and to a lesser extent by capital markets. Such interventions have provided long-term direct credit at affordable rates, as well as credit enhancements that seek to catalyze and unlock private funding for infrastructure<sup>13</sup>.

<sup>11</sup> This data is available at the World Bank Group. Private Participation in Infrastructure Database. Available in: <https://ppi.worldbank.org/data>.

<sup>12</sup> The paper considers the PPP concept used in the PPP Reference Guide which is: “A long-term contract between a private entity and a governmental entity, to provide a public asset or service, in which the private agent assumes a significant part of the risks and management responsibility and the remuneration is linked to the performance”. World Bank Group; Private Infrastructure Advisory Facility; Asian Development Bank; Inter-American Development Bank; Multilateral Investment Fund. Public-Private Partnerships Reference Guide, version 3, 2017.

<sup>13</sup> World Economic Forum. *Strategic Infrastructure: steps to prepare and accelerate Public-Private Partnerships*, In Collaboration with the Boston Consulting Group, May 2013, page 14.



There is evidence that significant private resources still seek opportunities to invest in well- prepared and structured infrastructure projects<sup>14</sup>. The financing gap may therefore be symptomatic of a larger *resource gap*. This resource gap can be explained by major PPP failures which are related to preparation and structuring issues<sup>15</sup>:

**Figure 4 – Public-Private Partnership failures and dry pipeline are particularly due to preparation issues**

	Project inception	Project preparation	Project implementation
Project-cycle related	<ul style="list-style-type: none"> <li>No integrated strategic plan &amp; long-term project pipeline</li> <li>Unreliable cost-benefit analysis</li> <li>Biased value-for-money analysis</li> </ul>	<ul style="list-style-type: none"> <li>Lack of preparation funding &amp; rigorous preparation process</li> <li>Biased demand &amp; cost forecasts</li> <li>Insufficient revenue sources &amp; lack of market sounding</li> <li>Stakeholder resistance</li> <li>Inadequate risk charing/ mitigation &amp; misaligned incentives</li> </ul>	<ul style="list-style-type: none"> <li>Uncompetitive, opaque &amp; slow tendering</li> <li>Overbidding &amp; renegotiation</li> <li>Opportunistic regulation &amp; termination</li> <li>Weak financial structure &amp; low operational performance</li> <li>Macroeconomic shocks</li> </ul>
Enabling environment related	<ul style="list-style-type: none"> <li>Weak public-sector capacity</li> <li>Poor legal &amp; institutional framework</li> </ul>	<ul style="list-style-type: none"> <li>Low local financial market &amp; local industry development</li> <li>Corruption</li> </ul>	

Source: WEF 2014

International efforts to help governments attract private investment by strengthening tools such as PPPs and other forms of private financing have been increasing in recent years. In 2015, the major MDBs signed a commitment to take practical steps to foster collaboration between MDB-based PPFs and governments. These steps would support the development of prioritized pipelines of social, viable and bankable infrastructure projects that can attract the private sector.<sup>16</sup>

<sup>14</sup> Quantifiable evidence is not easy to find, however the Mckinsey Global Institute analysis concluded that a largest constraint seems to be the lack of well-prepared projects. Mckinsey Global Institute. Bridging Global Infrastructure Gaps. June 2016, pages 17-18.

<sup>15</sup> World Economic Forum. *Strategic Infrastructure: steps to prepare and accelerate Public-Private Partnerships*, In Collaboration with the Boston Consulting Group, May 2013, page 18.

<sup>16</sup> G20. Paper prepared by MDBs for Circulation to G20 Development Working Group and G20 Investment and Infrastructure Working Group. *Partnering to build a better world: MDB's common approaches to supporting infrastructure development*. 18 September 2015, pages 9 10.

The PPP market in LAC is highly concentrated in Brazil (65%), followed by Mexico (11%), Colombia (7%), Peru (6.4%) and Chile (5.3%). However, the readiness of the PPP environment varies greatly across the region, and an important challenge is the high rate of contract renegotiations in LAC in recent decades. These renegotiations themselves may be the result, in some cases, of poor project preparation. Risk misallocation is often at the center of renegotiation processes, suggesting poor project preparation and deficient value-for-money (VfM) assessment, together with incomplete contracts or regulatory weaknesses. All of these factors significantly alter the desired project results.<sup>17</sup>

## 1.2. IDB and the PPPs

The IDB's updated Institutional Strategy (IS) outlines the main challenges the LAC region will face in the coming years and defines how the Bank will address these challenges. The IS aims to ensure that infrastructure services are present in all three pillars. In this context, according to the IS, the Bank will help countries to:

- **Improve social inclusion and reduce inequality** by *providing inclusive infrastructure services*, including in urban areas, focused on the poor and vulnerable, in conjunction with factors such as transportation infrastructure, safe and stable provision of energy, safe drinking water and adequate social infrastructure (particularly hospitals and schools).
- **Increase productivity and innovation** by *providing urban planning and rural infrastructure*, especially infrastructure services in urban centers (which requires municipal planning and regulation) and infrastructure to rural communities, which will lead to higher productivity, increased earnings for agricultural workers, and better food supplies.
- **Increase economic integration** by *improving regional infrastructure*. This includes investments in transportation, telecommunications, and energy infrastructure both within and across borders. Those investments provide ample scope for public-private and regional inter-governmental collaboration.

Furthermore, the IS also includes an important element of the Bank's vision to improve engagement with external stakeholders, including the private sector. According to the IS, the Bank will improve and increase its development support through the private sector. Because of its convening power and reputation as a long-term trustworthy institution with technical knowledge, the Bank is able to bring public and private sectors together and engage them in different PPP models such as: public finance works, leasing, joint ventures, and long-term concessions to share risks and broaden investment horizons.

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<sup>17</sup> Inter-American Development Bank. *Evaluation of Public-private partnerships in Infrastructure*, Office of Evaluation and Oversight, 2017, page 9. Available in: <https://publications.iadb.org/handle/11319/8200>.

Based on the Bank's experience in working with governments to attract private participation in infrastructure through PPPs<sup>18</sup>, and based on benchmarks established in other regions, the key challenges for successful PPPs are as follows:

- A Legal frameworks.** Successful PPP initiatives are highly correlated with clear frameworks that define the role of the public and private sectors, delegating responsibilities such as risk management for investors, PPP feasibility assessments, accountability and transparency. In recent years, LAC countries have demonstrated progress in this regard by reforming or creating new concessions and PPP laws. However, there is still room to improve these legal frameworks to make them competitive in the eyes of international investors.
- B Institutional capacity.** Public agencies must possess the capacity to identify, formulate, evaluate, prepare, structure, contract and supervise PPPs projects to make these projects sustainable in the long term. Many countries in LAC have modernized their institutional setting to prepare and manage PPPs projects. However, particularly in low income countries and at sub-national levels, institutional capacity must be further improved.
- C Fiscal aspects.** Even though PPPs are designed to face constraints that many states encounter, it is important to manage the range of contingent liabilities that arise from various projects. Countries need to be able to estimate and manage project risks and plan accordingly before engaging in major PPP programs. Very few countries in LAC plan for these risks sufficiently.
- D Sector regulatory framework.** The regulatory environment at the sector level are as important as the overall legal framework. Clear regulatory rules regarding tariffs, competition, investments and service are key to attracting private investment.
- E Prioritization and project preparation.** A clear pipeline of projects is important to signal private sector expectations for future deals. In addition, project preparation and structuring are critical for improving project quality and reducing risks to both public and private investors. The LAC currently lacks effective long-term planning of this kind and cannot attract outside investment in advance of projects until it uses the PPFs that have been effectively utilized in other regions.
- F Credit enhancement instruments and capital markets.** Mechanisms to transfer risk serve as important complementary elements for PPPs. Insurance for political risk, credit guarantees and other instruments are essential for making projects bankable and attractive to institutional investors.

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<sup>18</sup> Inter-American Development Bank. The 2017 Infrascope: evaluating the environment for public-private partnerships in Latin America and the Caribbean, 2017. Available in: <https://drive.google.com/file/d/0B9ZrLkK2JshXUINoQ21iLXAwWTQ/view>

A recent evaluation by the IDB Office of Evaluation and Oversight (OVE)<sup>19</sup> regarding the IDB's operations that involve public-private partnerships concluded that the IDB has been very active in the PPP space. The Bank has been particularly effective in promoting favorable environments for infrastructure projects, but not in project preparation. As a result, the Bank has recommended the use of new advisory products, such as the PPFs. While the IDBG approved, during the 2006-2015 period, around \$900 million (USD) for 77 *enabling environment* operations and \$4.9 billion (USD) for 58 financing operations, the amount provided for *project preparation* operations was a mere \$9.4 million (USD), or around 0.2%, for 10 different projects. It is important to note that the economic yield of a *project preparation* operation performed with the assistance of the IDB is arguably more effective at attracting and leveraging funds to a project in the LAC region than pure financing, given the IDB's sterling reputation in the region.

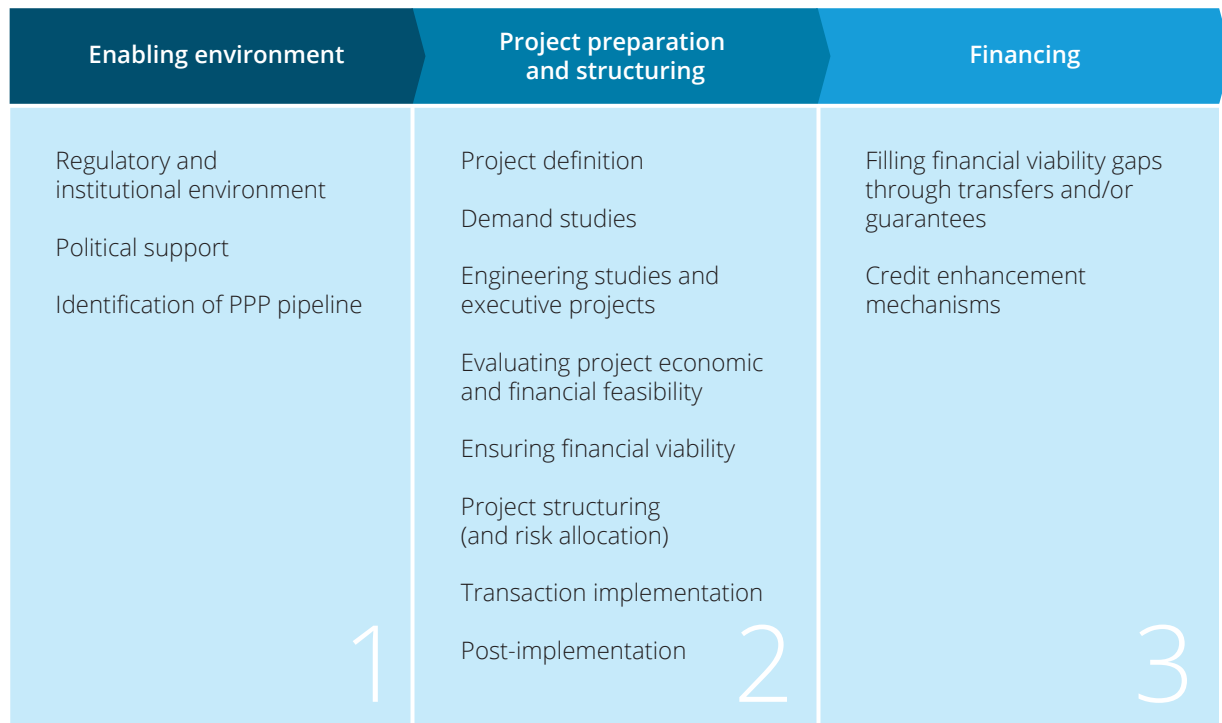
Thus, this paper deals how the IDB can best improve its work in reducing the resource gap. To this end, in Chapter 2 this paper presents an overview of other MDBs' PPFs, as an outline to help countries to prepare and structure well-established projects. In Chapter 3, the IDB experience with PPFs is analyzed; in Chapter 4 conceptual considerations are made for the design of future PPFs in the IDB and finally Chapter 5 offers general recommendations on how to implement a PPF at the IDB.

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<sup>19</sup> Inter-American Development Bank. Evaluation of Public-private partnerships in Infrastructure, Office of Evaluation and Oversight, 2017, pages 41 and 43. Available in: <https://publications.iadb.org/handle/11319/8200>.

## 2. Overview on MDB's PPFs

What are the elements required to achieve a well-prepared project? These necessary ingredients can be ordered by their chronology within a projects development, as each stage of the process requires different elements to achieve success. The figure bellow illustrates the three different stages<sup>20</sup> and their most common components



The enabling environment (also defined as upstream activities) is the set of conditions that are required for a country to promote a successful PPP. Usually, these conditions include the regulatory environment, rules and boundaries on how PPPs are implemented and political support. Of these, the political will to implement a PPP project within the federal, state and even municipal levels is the most important. The reality in most developing countries is that in the rush to establish new projects, governments overlook the need to enact the proper enabling environment for infrastructure development resulting in inadequate regulatory certainty and sometimes a lack of broad-based political support.<sup>21</sup>

<sup>20</sup> The three different stages are described below. It is important to stress that the stages described, and its components are based - in good extent - on the Reference Guide. World Bank Group; Private Infrastructure Advisory Facility; Asian Development Bank; Inter-American Development Bank; Multilateral Investment Fund. Public-Private Partnerships Reference Guide, version 3, 2017..

<sup>21</sup> G20 Development Working Group. *Assessment of the Effectiveness of Project Preparation Facilities in Asia*. Adam Smith International, September 2014, pages 3-4.

Project preparation and structuring, also known as downstream activities, is a crucial phase and it includes identifying a project, evaluating the project's economic and financial feasibility, allocating risk between the public and private sector, and finally implementing the project.

Developing countries often lack institutional and technical capacities in developing (preparing, structuring, tendering, contracting and supervising) PPP projects. This is often a result of the unique requirements of PPPs, which differ in comparison to those required for more traditional public procurement.<sup>22</sup>

Finally, the third stage includes all measures related to financing the project such as closing any financial viability gaps and establishing credit enhancement mechanisms, where necessary.

Based on these three stages, this chapter will examine how three PPFs in MDBs have been trying to help countries in preparing and structuring successful public infrastructure projects with PPP mechanisms and to what extent they have succeeded. Some PPFs will cover all the three stages presented, whereas others will focus on one or two phases only.

The selection of these institutions and their respective PPFs is relevant for several reasons. First, the most relevant PPFs are at institutions that are functionally similar to the IDB in the areas of infrastructure development. Second, like the IDB, all of these institutions have sought to address the lack of successful public-private infrastructure projects through interventions at the institutional level. Finally, all of these facilities were launched in the last few years spurred on by the same motivating factors that have moved the IDB. Therefore, these examples are the most relevant as a predictor of the type of impact the IDB could have. It is important to note, however, that these facilities are new and are still evolving in their capacity and approach. Furthermore, since these facilities only began their work in the recent past, it is difficult to assess the viability of their efforts in a rigorous, quantitative manner.

Project preparation, structuring and advisory activities are also performed in other development institutions, and some of these other programs can be found in Annex 1.

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<sup>22</sup> World Economic Forum Strategic Infrastructure: steps to prepare and accelerate Public-Private Partnerships, In Collaboration with the Boston Consulting Group, May 2013, page 18.

## 2.1. Overview<sup>23</sup>

The three facilities studied are: the Asian Development Bank (ADB)'s Asia Pacific Project Preparation Facility (AP3F)<sup>24</sup>, the European Bank for Reconstruction and Development (EBRD)'s Infrastructure Project Preparation Facility (IPPF)<sup>25</sup> and the Global Infrastructure Facility (GIF) chaired by the World Bank Group (WBG)<sup>26</sup>. The information contained in this section are based on public documents and interviews with the facility's staffs<sup>27</sup>. Additional information about these PPFs is available in Annex 2.

Figure 5 – ADB, EBRD and WBG Facilities Overview

Facility	Asian Development Bank (ADB)	European Bank for Reconstruction and Development (EBRD)	Global Infrastructure Facility (GIF)
Objective	Promote quality infrastructure projects	Promote quality infrastructure projects	Close infrastructure gap through mobilizing private capital
Stages:	Enabling environment Project preparation Financing	Enabling environment (Public window) Project preparation (PPP window)	Prefeasibility & enabling environment (PDA) Project feasibility and transaction structuring (PPSA)
Donors/Source of funds	Australia, Canada and Japan	EBRD ordinary capital	Australia, Canada, China, Japan, Singapore, WB
PPF Capital (estimate)	US\$ 73M	EUR\$ 40M	US\$ 90M
Facility type	Non reimbursable Reimbursable	Non reimbursable Reimbursable	Non reimbursable Reimbursable
Type of Projects	PPPs	Public Sector PPPs	PPPs
# of PPP Project preparation and structuring	4	3	27 in Stage I (PDA); 14 in Stage II (PPSA)
Staff	Representatives from the operations departments, chaired by the head of OPPP	4 project preparation managers 1 secretarial support staff 1 PPP policy expert 1 infrastructure policy expert.	9 full-time technical staff; 1 manager; 1 operations analyst.
Sectors typically covered	Transport Urban Development Energy Social Infrastructure	Transport Energy Water	Transport Energy Water & Sanitation Telecommunications

<sup>23</sup> All the information regarding the facilities was collected in 2017-early 2018.

<sup>24</sup> Asian Development Bank. Establishment of the Asia Pacific Project Preparation Facility. October 2014.

<sup>25</sup> European Bank for Reconstruction and Development. Proposal for an EBRD Infrastructure Project Preparation Facility. 2015.

<sup>26</sup> The GIF is a partnership among governments, multilateral development banks, private sector investors, and financiers. It is designed to provide a new way to collaborate on preparing, structuring, and implementing complex projects that no single institution could handle on its own. Its governing council comprises representatives of funding and technical partners as well as representatives of emerging markets and developing economies, and is co-chaired by the WBG and a funding partner. More information is available at: <http://globalinfrafacility.org/>.

<sup>27</sup> We would like to specially thanks the support of Almaz Galiev and Trevor Lewis from the ADB; Matthew Jordan-Tank from the EBRD and Jason Zhengrong Lu, Rob Pilkington, Shuai Ren and Matt Bull from the GIF.

### **2.1.1. Objective**

All PPFs examined here share a common goal to promote quality infrastructure projects. While the EBRD PPF also supports the preparation of purely publicly financed projects, the ADB PPF, in addition to supporting the classical infrastructure sectors, also supports the preparation of social infrastructure projects such as schools and hospitals.

The ADB PPF (also known as AP3F) was created to address five major challenges that currently impede greater private infrastructure investment (i) inadequate deal flow; (ii) a weak enabling environment; (iii) an inappropriate predetermined approach; (iv) poor quality advice; and (v) a complex regional agenda.

Some of the objectives driving design of the EBRD's IPPF are: (i) promoting more efficient delivery of projects with improved quality; (ii) strengthening local capacity for EBRD public sector clients; and (iii) delivering greater private sector investment replicability through policy dialogue and better knowledge exchange.

The GIF hosted by the WBG endeavors to create a collaborative platform to build consensus, offer advice, and seek commitments towards bankable infrastructure projects. For this purpose, it was able to coordinate MDBs, the private sector and investors.

### **2.1.2. PPFs' Role in the infrastructure process**

As discussed before, most PPFs cover upstream and downstream activities. The AP3F and GIF also cover downstream activities not usually covered by other facilities including market sounding and credit enhancement. Those latter activities can be found in the third stage of the infrastructure development process.

The ADB has established four pillars to address PPP projects: (i) capacity development (ii) enabling environment; (iii) project preparation; and (iv) financing. In order to achieve this, AP3F supports: (i) upstream sector reforms (enabling reforms and capacity building); (ii) due diligence; (iii) preparation of information memoranda and marketing; and (iv) attracting high-quality sponsors by preparing strong project documentation and robust financial models.

The AP3F is directly linked to the Office of Public-Private Partnership (OPPP), which is supervised by the managing director, in accordance with the ADB organizational structure. AP3F was launched in January 2016. As of April 2017, 11 applications for AP3F support have been approved and 4 of these applications (\$4.5 million) are for project preparation assistance. None of these projects have been closed.

The IPPF PPP window will mainly focus on technical, financial and legal due diligence to enable project sponsors to develop bankable deals with clearly identified revenue sources and appropriate allocation of risks. The IPPF was incorporated within the Infrastructure Business Group (IBG), which is led by the IBG Transition Unit.



The initial IPPF goal for its first 3 (three) years - from September 2015 to August 2018 - was to prepare and award 10 Projects in their PPP Window. As of May 2017, the IPPF had 3 projects in their PPP Window and 8 projects in their pipeline. These projects now await government approval.

The GIF's portfolio has grown significantly since it began its operations in April 2015, with 41 activities totaling US\$36.1 million to funding support. As of June 2018, the GIF has a portfolio of 14 PPSAs and 27 PDAs in diverse sectors, at varying stages, from regions across the world. Total mobilization, if all 41 GIF-supported projects reach financial close, is expected to reach US\$39 billion, of which approximately half is expected to come from the private sector.

### **2.1.3. Preparation and Structuring Period**

According to ADB, the estimated period for the preparation and structuring of each project varies significantly depending on the specific circumstances and readiness of each project. One of the projects (10-month input), for instance, has already been prepared and structured by a transaction advisor funded by the government. AP3F is supporting legal due diligence under the project involving: i) preparation of template and project specific concession agreements; and ii) operational support to the grantor during the tendering period, up to commercial close.

In EBRD they expect 24-30 months to the closure of the contract and finance mechanism. And each project is expected to cost approximately 2 million dollars.

The preparation period for GIF applications ranges from two months to six months. GIF review and approval takes place on a rolling basis, starting upon receipt of the completed application and government letters of support. The approval process usually takes several weeks (in the case of requests over \$500,000 which need to be submitted to the GIF Governing Council for no-objection). In terms of estimated periods to commercial close, the average is about 20 months.

The GIF support is provided in three main products:

- Project Readiness Assessment (PRA) is a standardized tool to quickly assess the completeness of project preparation to date and identify the most appropriate type of GIF support to deploy.
- Project Definition Activity (PDA) is a non-reimbursable grant typically of up to 150 k (USD) for early stage project scoping and definition support providing governments with the information necessary to decide whether to proceed to full feasibility and transaction structuring.
- Project Preparation & Structuring Activity (PPSA) provides up to several million dollars of generally reimbursable support to fund full project preparation and transaction structuring, taking the project to commercial and, in cases, financial close.

#### 2.1.4. Administrative process and other relations

In the case of the AP3F, a working group made up of representatives from the operations departments, chaired by the head of OPPP, reviews and makes recommendations on proposals for the facility. The AP3F manager coordinates with the regional departments' national PPFs, as well as special purpose vehicles and technical assistance programs already being used to prepare PPP projects in Developing Member Countries (DMCs). The AP3F works alongside existing PPFs and, when appropriate, collaborates with them on specific projects.

The AP3F team consists of two international staff, three international consultants and two national analysts. AP3F plans to hire five more consultants by the end of 2018

When the AP3F team receives a statement of Interest for AP3F support (project description), the relevant regional department (RD) and resident mission (RM) confirm their support and nominate a focal or focals, who will be responsible for coordinating the preparation of the application by the client and subsequent monitoring of the activity. If the RD / RM are not interested, the AP3F team will work directly with the client. The relevant RD and RM shall nominate a focal point to monitor the transaction prior to the approval of the application by ADB.

According to the AP3F Implementation Guidelines, AP3F may support "DMC governments and their public-sector agencies, including central and local governments, government agencies (including sub-sovereign and government-owned entities), and other entities eligible to receive assistance.

AP3F has yet to be approached by National Development Banks for assistance.

The IPPF is currently working with a staff of five people: (i) the IPPF manager for both its public and PPP window; (ii) a public window manager; (iii) a PPP window manager; (iv) a PPP expert and (v) an analyst. In addition to this staff, there are sector specialists within the EBRD who assist by revising the Terms of Reference of the consultancies, The PPP window staff negotiate the agreement between the facility and the government and participate in the most important meetings with the consultants.

The IPPF structure also includes eight pre-selected consulting firms that signed framework agreements to perform specific individual call-off assignments. Upon request to proceed with the preparation of any given project, the call-off consultants are expected to mobilize within three to four weeks.

The GIF team, based in Washington DC, Singapore and Tokyo, as of June 2018, is comped by: 9 full-time technical staff, 1 manager, and 1 operations analyst.

Implementation of GIF project activities will be led by technical partners. Project teams will comprise technical staff from the GIF's Technical Partner, as well as the engineering, financial, economic, or legal firms hired with GIF resources. GIF staff can, as required, join the implementation team and provide complementary sectoral expertise and skills at the demand of a particular project. Joint project teams (for example, IFC and World Bank, or EBRD) may also be formed if the GIF is supporting projects in which more than one technical partner is already closely involved, or as needed to meet the full range of demands of the project.

The Technical Partners (TPs) through which GIF support is executed comprise the major MDBs: African Development Bank (AfDB), Asian Development Bank (ADB), European Investment Bank (EIB), European Bank for Reconstruction and Development (EBRD), Inter-American Development Bank (IDB), International Finance Corporation (IFC), and World Bank (WB). The Asian Infrastructure Investment Bank (AIIB), Islamic Development Bank (IsDB), and the New Development Bank (NDB) currently participate as observers.

### **2.1.5. Financing**

All PPFs were designed as a revolving fund that disburses and recovers all or part of its assistance for project preparation activities and subsequently recycles its capital. Likewise, all MDBs and other PPF partners may consider financing projects that have received their assistance. Conflicts of interest are addressed in the PPFs by-laws.

The AP3F is supported by Australia, Canada, and Japan. The ADB can accept further untied grant contributions from bilateral agencies, national government agencies, and foundations, including corporate foundations. It can also consider other types of contributions from fund contributors. ADB's Office of Co-Financing Operations will facilitate and help raise contributions to the fund and will act as the official channel of communications for financial issues between contributors, the ADB, and the AP3F. All project preparations supported by AP3F are funded on a 100% cost-recoverable basis. All capacity building and monitoring/restructuring activities are funded on a grant basis.

The IPPF is fully financed for at least the initial three-year period, with a net income allocation from the EBRD for other purposes. The funds made available to the IPPF complement EBRD's existing bilateral or multi-donor funds and other multilateral funding sources, such as the various European Union (EU) instruments.

The GIF became operational in April 2015, with an initial capitalization of US \$90 million. The first three years of GIF operations constitute a pilot phase, during which the GIF concept, activities, and partnership model will be tested.

### 2.1.6. PPF identified areas for project success

GIF highlighted four major areas necessary for the facility success:

- Projects need advocates within client governments who can focus on mobilizing resources during project preparation and implementation. GIF has been working with other trust funds (e.g. PPIAF) to help technical partners develop capacity amongst both the technical and political levels in governments. In cases where capacity building is closely related to transactions, GIF also allocates limited funding to ensure the governments benefit from “learning by doing”.
- Projects need experienced technical partner teams with knowledge of PPP / private finance. To support governments in bringing prepared, structured and bankable infrastructure projects to market, GIF not only provides funding to technical partners for procuring required skills, but also provides complementary technical expertise (e.g. transaction structuring, project financing, etc) to the project implementation team. This is particularly relevant for TP teams with strong sector knowledge but limited experience with private finance and transactions.
- Projects need to consider the full range of mechanisms to mobilize private finance for infrastructure. GIF approved activities concentrate on enabling private financing in creating specific infrastructure assets, and in most cases utilizing a PPP model. Recently, GIF worked with technical partners on other ways to mobilize private capital including project bonds, credit rating advisory, loan refinancing, transit-oriented development and land value capture, etc. The support focuses on ensuring not just one successful transaction but establishing steps towards a robust and sustainable long-term market.
- Projects need to close the knowledge gap between governments and the market. Comprehensive project support provided by the GIF draws on the combined expertise of its technical and advisory partners. The group of advisory partners includes commercial banks and institutional investors, and is often used as a sounding board to ensure that well-structured and bankable infrastructure projects are brought to market.

The ADB also described a lesson learned during their procurement experience: the AP3F team had initially attempted to set up a framework consultancy contract for all AP3F supported assignments with the goal of shortening consultants’ mobilization period. The selection process had to be cancelled. Separate framework contracts must be established for capacity building and project preparation activities as these may conflict. Several commercial banks / TAS providers expressed strong interest in being shortlisted under the framework for project preparation activities. This raised concerns related to fair competition and pricing arrangements under the framework given that it is not unusual for commercial banks to price their offers on a discounted retainer basis, where part of the cost of the project preparation is pushed to the success fee.

Where ADB provides TAS to a client, given that the relevant ADB TAS team manages all consultants under the project, the legal, technical and financial services required for the project delivery are procured separately using a combination of time-based, lumpsum and target priced arrangements. All TAs for project preparation incorporate a capacity building component or components, such as upstream legislative and regulatory reform and staff training.

The EBRD PPP window works on a 100% reimbursable basis from the private sector when it wins bids, plus a 10% fee that the government must pay to the IPPF during the project preparation process. This 10% fee was intended to more actively engage governments in the process, but it has proven prohibitive for many states. Nevertheless, the EBRD PPP will continue with this model at least for the initial 3 years period.

### **2.1.7. Relationship between Facilities**

The EBRD has been using GIF money to stretch its financial capacity. After successful close of the project, EBRD is reimbursed by the private sector and they return the borrowed amount to GIF.

### 3. PPFs and the IDB

This section discusses the IDB’s approach to PPFs, highlighting the experience of InfraFund and two PPFs funded with its resources: PSP Brazil and the Regional Public Advisory Program.

#### 3.1. Rationale for PPFs at the IDB

Design and implementation of PPFs at the regional and country level can support IDB’s mandate, as stated in the new IS, helping it to achieve: (i) economic integration; (ii) access and affordability, in particular to quality services; and (iii) increased support to the private sector.

The IDB has a comparative advantage in upstream activities now recognized as crucial to the successful execution of downstream activities, such as project preparation as well as the financial closure of deals. Figure 12 illustrates the opportunities for IDB support of PPPs:

Figure 6 – Strengths and Opportunities

STRENGTHS	OPPORTUNITIES
<ul style="list-style-type: none"><li>▶ Solid project preparation funds for publicly financed projects</li><li>▶ Strong country presence (decentralized)</li><li>▶ Technical capacity of sector specialists</li><li>▶ Good reputation with relevant governments</li><li>▶ Supporting PPP upstream activities</li></ul>	<ul style="list-style-type: none"><li>▶ New institutional strategy</li><li>▶ Restructuring private sector window (Inter-American Investment Corporation-IIC)</li><li>▶ Leverage partnership with other MDBs to complement the range of services</li><li>▶ Leverage partnerships with national development banks and local facilities (ex: BNDES, FDN)</li></ul>

To this end, the PPF has been instrumental in IDB’s strengthening of its position in providing innovative solutions to the public and private sector with end-to-end services: (i) helping governments strengthen their institutional framework and technical capacities, identifying projects and getting them into the project pipeline; (ii) ensuring high quality projects; and (iii) financing both the public (IDB) and private sector (BID Invest) components in a PPP project. The IDB project in Mato Grosso in Brazil is a good example of this end-to-end approach (see box below).

## Mato Grosso

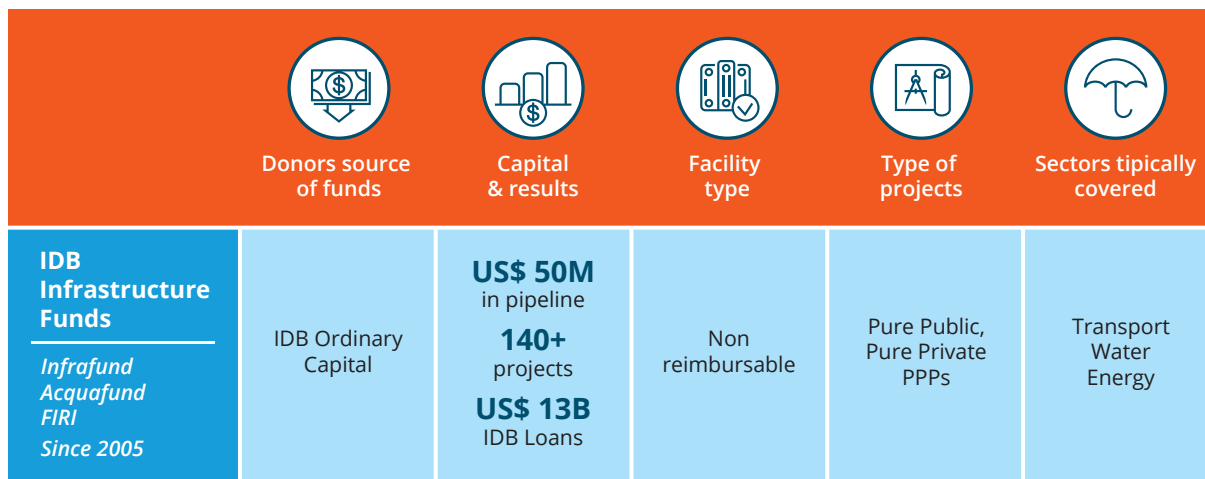
In May 2016, the IDB was invited by BNDES to take part in a discovery mission to Mato Grosso State, Brazil. The mission's purpose was to identify how the two banks could work together to help promote concessions and PPP in the state. The mission revealed that the State Government of Mato Grosso needs technical and financial support not only in its downstream activities, but in its upstream activities as well. For instance, Mato Grosso does not have an identified pipeline of PPP or concession projects or a regulatory agency to supervise projects that are built/operated by the private sector.

IDB's PPFs are also important because they are instruments that allow the Bank to guarantee that projects are well-prepared and aligned with the priorities and objectives approved by the member countries and stated in the IS. These objectives include fostering the development of sustainable infrastructure (environmental, social and economic) and enabling economic integration among LAC countries.

### 3.2. InfraFund

The Infrastructure Fund (InfraFund)<sup>28</sup> was created in 2006 to support project capacity building, preparation, financing and structuring in IDB's countries of operation to achieve sustainable infrastructure projects. For this reason, the IDB Board allocated more than US \$80 million of its ordinary capital since InfraFund's inception. Relevant figures are captured in Figure 6:

Figure 7 – Infrafund Main Results



Even though the majority of projects supported by InfraFund included traditional public investment, some of the fund's specific goals leveraged infrastructure investments across the region by enhancing the private provision of infrastructure. In order to do this, InfraFund

<sup>28</sup> InfraFund: <<https://www.iadb.org/en/about-us/project-preparation-facilities%2C6010.html>>.

promoted a series of technical cooperation project agreements, serving as an incubator for secondary's PPFs. Figure 6 illustrates the investment made by InfraFund in technical cooperation and Figure 7 shows that many technical cooperation agreements were not related to a specific loan, as an indicator of funding to purely upstream activities.

Figure 8 – InfraFund Technical Cooperation (TC) approvals

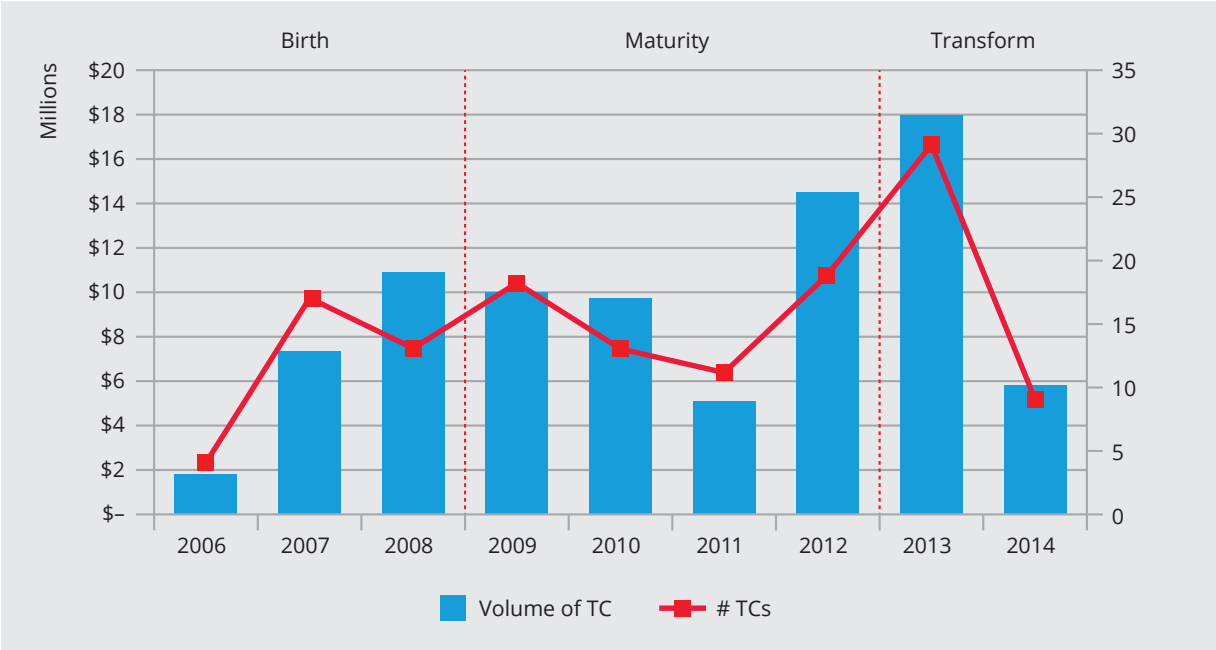
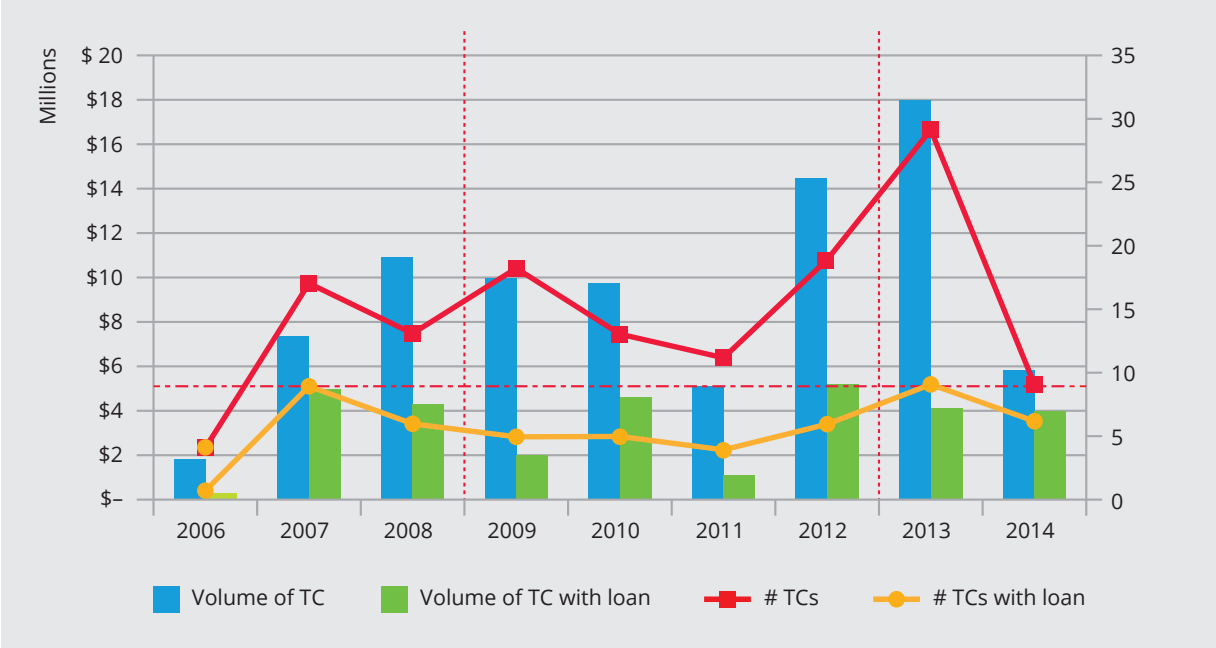


Figure 9 – Impact of InfraFund TCs on IDB loan portfolio





### 3.2.1. PSP Brazil

The Brazilian Private Sector Participation (PSP) Facility is one of the flagship initiatives IDB supports to improve project preparation. It was established with resources from the InfraFund, the IFC and the Brazilian National Development Bank (BNDES). The facility aims to enhance private sector participation in infrastructure projects in Brazil.

With total capital of US \$12 million, the facility helps structure projects from the planning stages through financial closing. Since its creation in 2007, this facility has supported 10 infrastructure projects, leveraging more than US \$6 billion in private investment. The facility is managed by the IFC, and it relies on the participation of the IDB and BNDES as part of its oversight committee. These institutions all have equal voting rights in selecting projects. BNDES is also active in project preparation and interactions with key counterparts.

Figure 10 – Past PSP Projects

Project	Year Concession Agreement Signed	Brief Description	Private Sector Investment Mobilized	Population Benefited	Main Features
BR 116/324	2009	Transportation: BOT of 680 km of roads linking the NE and SE of Brazil	US\$615 million	912,500	The project's contractual structure, based on performance, influenced the model used for seven road concessions in Brazil (totaling over 2,600 km)
BA 093	2010	Transportation: BOT of 126 km of roads	US\$400 million	2,500,000	1st concession structured for a network of roads surrounding the metropolitan area of a city
Hospital do Subúrbio	2010	Healthcare: full PPP of a 298-bed emergency hospital, DBFO	US\$50 million	400,000	1st Health PPP in Brazil, pioneer of several other health PPPs in the country.
BH Schools	2013	Education: PFI of 32 kindergartens and 5 elementary schools, DBFO	US\$100 million	18,000	1st Educational PPP in Brazil.
BR Airports	2013	One transaction encompassing two major international airports in Brazil (Galeão and Confins)	US\$3.2 billion	7,000,000	2nd Round of Airport concession in Brazil.
<b>Total</b>			<b>US\$4.365 billion</b>	<b>10,830,500</b>	

Source: PSP 2017

Figure 11 – Current PSP Projects

Project	Year Concession Agreement Signed	Brief Description	Private Sector Investment Mobilized	Population Benefited	Main Features
BH Primary Care	2015 (exp.)	Healthcare: PFI of 74 primary care units in the municipality of Belo Horizonte	US\$220 million	1,700,000	1st PPP involving Primary Care Units in Brazil.
Diagnostic Imaging Network (BA)	2015 (exp.)	Health: Imaging and associated Telemedicine project and Hospital Information System (HIS) study.	US\$68 million	4,321,830	1st Imaging and Telemedicine PPP in Brazil.
BR Amazon Forest	2015 (exp.)	Forestry: concession of sustainable forest management in forest areas in the Amazon region	US\$33 million	TBD	1st large scale tropical forest concession in Brazil.
<b>Total</b>			<b>US\$321 million</b>	<b>6,021,830</b>	

Source: PSP 2017

The experience with the PSP facility is the closest example, within the IDB, of the facilities described in Chapter 2. However, it is important to highlight that: (i) it does not cover upstream activities; (ii) it is intended to create solutions for a specific country, not for the entire region; and (iii) it is not entirely managed by the IDB and (iv) it does not establish financing support. It is correct to affirm that from all the three stages described in Chapter 2 on the infrastructure development process, the PSP only covers the second stage: project preparation.

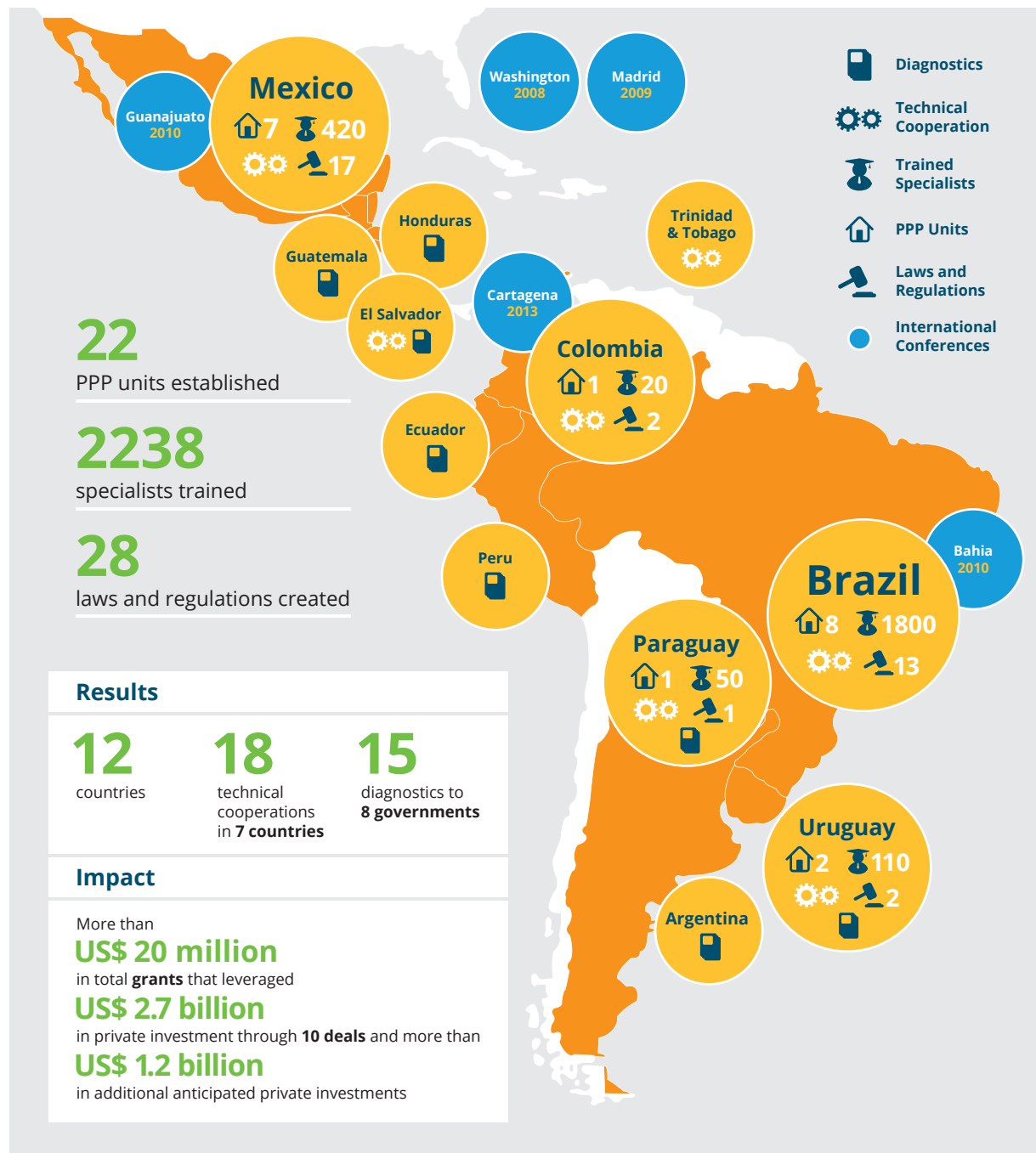
### 3.2.2. The Regional Public Advisory Program

The program was founded as a partnership between the Multilateral Investment Fund (MIF) and INE, financed through the InfraFund, to strengthen government capacity in preparing and implement PPPs using a new modality of advisory services.

The program focuses on national governments in small and less-developed countries, and other governments at the sub-national level that lack of institutional and technical capacity. The program brings a greater focus on bringing individual PPP projects to market and financial closure. Program activities include training in PPP policy frameworks and the development of non-financial products for project financing, project management and monitoring. Capacity-building services are provided directly to government institutions, so they can identify and manage PPP projects themselves in the future.

The program also provides a PPP knowledge exchange network to share and disseminate information generated about the development of PPPs. The network enables users in the region to access high-level research and knowledge products and exchange lessons learned. The major achievements of the program can be found below:

Figure 12 – The Regional Public Advisory Program in numbers



The program can be understood, as viewed in Chapter 2, as the first stage of the infrastructure development process. In other words, the program focusses on the enabling environment.

### **3.3. The role of PSP at IDB**

Several actors have played important roles in both upstream and downstream activities. The Regional Public Advisory Program, a partnership between the MIF and INE, built knowledge and capacity and helped establish the framework for the development of PPP projects. This capacity building addresses mostly upstream activities such as: strengthening the legal and institutional frameworks, improving technical capacities and identifying PPP projects for the future. In contrast, the scope of the PSP is mainly downstream activities, such as: technical, socioeconomic, financial and legal viability studies, and the design of bidding documents including the PPP contract model and transaction advisory services.

### **3.4. Administrative process**

The PSP is operated by the Infrastructure and Energy (INE) Department at IDB. The facility is governed by a board of donors consisting of one member from each donor (BNDES, IFC and IDB), which has the authority to grant simple majority approval to: (i) projects under consideration by the fund; (ii) budget ceilings for project consultants; (iii) the project execution advisor for each PSP project; and (iv) the fund's annual financial statements. The IFC, trustee of the PSP was initially allowed to select: (i) one investment officer to serve as facility manager; and (ii) one or two additional investment officer(s) or analyst(s) to be dedicated to the facility. This staff is based in the IFC office in Sao Paulo, Brazil.

### **3.5. Counterpart participation**

It is important to highlight that there are two groups of countries within the LAC region that require different approaches and support from the IDB. The first group is made up of medium-income countries with a mature PPP environment that in most cases, have a steady pipeline of projects (e.g. Chile, Brazil, Peru, Mexico and Colombia). These countries have a stable and operational PPP environment so, while they do require IDB support, most of the legal, technical and financial advisory services provided are at the project level. The second group is composed of mainly medium- to low-income countries where the PPP environment is still in its initial phase. In these environments, support from the Bank is primarily in developing favorable legal and institutional frameworks, and identifying potential pilot projects for proof of PPP concept.

It is also important to note that some countries will likely have national counterparts willing to participate in a PPF. The PSP is an example of this, as it is 49.96% funded by BNDES. In cases such as these, regional PPFs have advantages because they can increase scale, reduce risks and thus assure the sustainability of the PPFs.

## 4. Recommendations of a PPF framework for the IDB

This paper highlights the importance of the IDB engaging in a new PPF framework in order to help countries prepare and structure successful infrastructure PPP projects that will attract the private sector. This investment in turn would reduce both the resource and infrastructure gaps. Based on the information gathered here regarding other PPFs MDB experiences, as well as the current project preparation experience within the IDB, the following PPF structure and framework should be considered by the IDB going forward. Even though these recommendations are based on the IDB context, in many cases can be valid for other contexts and MDBs.

### 4.1. Scope

One of the key objectives for strengthening the role of PPFs in the IDB is to align existing instruments (e.g. technical cooperation and fee for service policies) and develop new ones to provide support for specific project requirements. To be truly effective, however, the PPF must ensure that there are no weak links in the entire project preparation chain. Therefore, we suggest that the IDB PPF, as GIF and AP3F, covers both upstream and downstream activities (first and second phases) as well as financing.

The figure below describes the three stages that the IDB PPP should cover, a recommendation, in accordance with what was examined in Chapters 2 and 3:

Strengthening the enabling environment

- » Legal and regulatory environment
- » Institutional environment (including improving specific PPP legislation, strengthening PPP units and line ministries)
- » Political support and advocacy
- Project development capacity at the appropriate level of government: federal, state and/or local
  - » Project identification, prioritization and definition
  - » Training and dissemination of knowledge and best practices
- Project development capacity within the public sector
  - » Evaluating project economic feasibility
  - » Ensuring technical, legal, and environmental compliance
  - » Conducting subsidy and affordability analyses
  - » Structuring the project (and allocating risk)
- Financing
  - » Implementing transactions

It is important to emphasize that additional preparation activities are required for all the stages mentioned above. Often PPFs only support a few of these stages with technical assistance and funds, leaving others uncovered. This could work if the other stages were being well-prepared. Therefore, if the PPF will only support some steps for a specific project, it must make sure that partner institutions have expertise and capacity in the other areas.

Upstream activities are usually more neglected during the project development phase, although as noted in both the OVE report and Chapter 3, they have been well implemented at the Bank. However, these upstream activities can still be enhanced. For instance, in areas such as contingent liabilities accounting and management, and other project-specific requirements, there is still room to grow. The creation of a new PPF framework serves this purpose: to create an end-to-end approach where the upstream work is connected to the project preparation and financing phases, in a coherent and efficient manner.

Necessarily then, an effective PPF will support the funding of both upstream and downstream activities. Activities related to disseminating information on the project, prospecting potential investors and credit enhancing could also be included.

## 4.2. Sizing the facility

One of the primary reasons for inadequate project preparation is the reality that the project preparation and structuring process is costly and long. For example, the average time to procure a PPP in the UK is 34 months, an average of 25 months for PPPs for schools, 38 months for PPPs for hospitals and 47 months for other PPP projects<sup>29</sup>.

Therefore, it is important that PPFs be designed and funded with this length and cost in mind. Relevant factors include:

- Average number of projects to be prepared and structured by the PPF
- Expected duration from conception to tender
- Maximum level of funding
- Non-reimbursable level of funding
- Expected rate of success (i.e. fraction of projects that reach financial close)
- Initial funding corpus of the facility
- Annual funding stream of the facility
- Number of staff members

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<sup>29</sup> Source: KPMG, "PPP Procurement Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects," May 2010

As an illustration (see Table 5), consider a PPF that is funded at the outset with US \$34 million and to which contributions of US \$2.75 million are made each year. If the preparation period of each project is three years, and the average project preparation cost is US \$2.5 million, with a 10% non-reimbursable component and a success rate of 50%, such facility can prepare two projects per year (PPF design A).

If the same fund reduces its level of funding or targets smaller PPP projects so that average project preparation costs are US \$1 million, it can prepare four projects per year and even allow a reimbursable component of 40% of project preparation costs (PPF design B). Furthermore, if the success rate of the same fund rose to 75%, it could even prepare five projects per year (PPF design C).

**Table – PPF Sizing**

PPF design		A	B	C
Initial fund size	\$m	34	34	34
Annual funding	\$m per year	2.75	2.75	2.75
Preparation period for each project	years	3	3	3
Average PPF funding	\$m per project	2.5	1	1
Non-reimbursable level	% of average funding	10%	40%	40%
Success rate		50%	50%	75%
Number of projects prepared	per year	2	4	5
Steady state fund size	\$m	19	21	19

This is the revolving fund model of a PPF where project preparation funds recovered from successful projects are invested back into the fund. At the same time, ongoing annual contributions maintain the shortfall created by the non-reimbursable component or the failure of projects. The annual contribution can come from the government or a development institution, but it can also be sourced from winning bidders of successful projects (though this will also lead to an increase in expected bid costs).

Given the length of the project development phase (assumed to be three years), the “steady state” size of the fund will be smaller than the initial size of the facility. For example, for PPF design A, the steady state size of the fund is US \$19 million.

### 4.3. Funding

As examined in Chapter 2, the IPPF, the AP3F and the GIF all fund upstream and downstream activities. The IDB can also fund both upstream and downstream activities as described below.



### 4.3.1. Funding upstream activities

It is not just host governments that fail to adequately fund upstream activities; it is also challenging to arrange when using a revolving fund. Paradoxically, it is because upstream activities typically benefit multiple projects that their expenses are the hardest to recoup from any specific project. As a result, it is prudent to recognize that the cost of upstream activities supported by the PPF will most likely not be reimbursable from successful projects.

Non-reimbursable expenses incurred by the facility should be restricted to a maximum level per project (say US \$1 million) or for the facility as whole (for example 20% of the facility capital). For the PPF to be sustainable, the host MDB would have to set up a funding mechanism by which annual grant funding would replenish the non-reimbursable expenses of the PPF.

An alternative mechanism to fund non-reimbursable activities is to mobilize support from the host government for each project. This can take the form of in kind grants (providing resources such as personnel and institutional capacity) or in cash. Mobilizing and securing host government funding from the public budget constitutes an explicit demonstration of commitment, aligning government incentives for choosing the most promising projects for preparation, and raising the likelihood that the project will reach tender stage.

A more advanced model can allow not just projects, but the facility itself to be funded by a specific country and is therefore dedicated to developing projects in that country alone. The PSP is an example of just such a facility and is based on size and local capacity. These types of funds can be effective in Brazil, Chile, Peru, Mexico and Colombia.

### 4.3.2 Funding downstream activities

Downstream activities can be funded using a revolving fund that would disburse and recover amounts for all or most of its activities and subsequently recycle its capital. In this case, the budgetary funding would only be required for the initial formation of the fund and for covering the cost of the preparation of projects that fail to reach tender stage.

The steady-state size of the facility represents the portion that can be funded using external investors in the form of debt and/or equity. Such a funding mechanism would also require: (i) establishing a governance mechanism for the facility; and (ii) incorporating a rate of return that can be financed by charging a success fee.

At the outset, and in the absence of a history the PPF, it appears difficult to attract external investors. Raising equity, however, would require sharing some of the facility's management control with external equity holders who would then have influence over where the institution would operate.

Furthermore, in the absence of tangible assets and a predictable cash flow, it is unlikely that the facility could raise debt without a counter guarantee of repayment from the host bank. In other words, any debt issued by the PPF will be little more than standard debt. Therefore, it would be best to wait approximately three years before evaluating the PPF's readiness to raise financing from external investors to refinance the existing facility or expand its size.

## **4.4 Administrative structure**

Even after the desired objectives and funding of a PPF have been described, it remains to be determined what its scope and capacity ought to be. In the broadest terms, this question will determine whether the PPF will perform most of the substantive activities itself, using its own personnel, like the model presented in the IPPF and GIF, or if it will serve as the manager in these activities, drawing upon resources outside the facility, as described in the AP3F model.

There are two possible ways to address this question. First, institutional capacity of various types – sectoral, legal, financial – within the PPF may suggest how many responsibilities its own staff can take on. If the facility is sized to prepare a total of two to five projects per year, it is unlikely that all the required expertise for a particular project resides within the fund. On the other hand, this is the model that would allow for the greatest impact on the quality of project preparation work.

The other limiting case might be one in which the PPF selects and contracts with outside resources – other departments within the bank, external consulting companies, financial and legal advisors – to fulfill specific tasks and studies as needed for each project. In this model, the role of the facility would primarily be that of senior manager and as an interface with the host government, and it would be able to perform these tasks with a relatively small number of full-time personnel.

In the view of the authors, the PPF should endeavor to maintain staff with the most relevant skills– those related to economic, regulatory, financial, legal and political analyses of infrastructure – within the facility. Outside sources can be relied upon for additional sectoral or specialized skills based on the needs of specific projects.

### **4.4.1. Governance of PPFs and interface with the government**

There are two models of PPFs: a single facility for all countries, or specific facilities for particular countries and/or sectors. All PPFs discussed in Chapter two are regional facilities.

The IDB currently possesses both regional and country specific facilities. Facilities like InfraFund cut across countries and sectors while other facilities are more specific (the PSP focuses on one country (Brazil), while the AquaFund focuses on one sector (water and sanitation). As the specificity of the fund increases, its depth of expertise on country or sector-specific issues will also grow.

The IDB should start by establishing a single facility that encompasses all countries and sectors. This facility would not only prepare projects across countries and sectors, but might also serve as an incubator for more country/sector-specific facilities. Once deal flow has grown sufficiently to sustain a small group of personnel with country/sector-specific skills (such as Brazil), such a facility can be separated from the parent fund, perhaps coupled with a significant development institution in the relevant country (such as BNDES in Brazil) and established as a separate unit. It is conceivable that countries such as Brazil, Peru, Mexico, Chile and Colombia could sustain country-specific PPFs. However, the benefits of regional or sectoral specificity must be balanced against the excessive fragmentation of skills and resources.

The experience with InfraFund's location within the IDB and its resultant focus should serve as a guiding example in establishing PPFs. A 2015 study concluded that while the InfraFund had been effective at promoting investment in infrastructure in a quarter of the IDB's countries of operation, it was less successful in increasing private sector participation or stimulating PPP. The study attributed this to the shift of InfraFund from the office of the Private Sector Coordinator to the Grant and Co-financing Management Unit (GCM) under Vice Presidency for Countries (VPC), where it "became more closely related to the Bank's own pipeline preparation activities (i.e., favoring public sector loans)."<sup>30</sup>

Because advisory services must be aligned to PPF governance, it is vital that the MDB that hosts the PPFs consolidates knowledge and technical skills among a few groups and establishes a work process that enables collaboration between multi-sectoral teams that are technically sound and responsive.

Conceptual engagement models for MDB can include the following actions: (i) consolidating a PPP response unit that serves as an initial point of contact with countries, prioritizing the use of technical and financial resources, and working as both the planning unit and a project management office; (ii) defining a work process to form ad-hoc teams led by someone from the PPP unit that can be assigned to respond to specific needs, remaining mindful of the fact that those assignments must have attendant proper incentives; and (iii) using the existing country offices as an advanced point of contact since the PPP unit must have resources in the country office, forming teams that include specialists in the field. The model used by the World Bank in Singapore could be considered a benchmark.

Finally, the development of PPP projects needs to be coordinated and aligned with each country's sector framework and strategy. This would require enhancing coordination among sector departments and divisions and between teams responsible for sovereign guarantee (SG) and non-sovereign guarantee (NSG) interventions. This would also require coordination with the "PPP unit".

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<sup>30</sup> Review and evaluation of InfraFund: A Report prepared for the Infrastructure Department (INE) of the Inter-American Development Bank, March 2015.

## 4.5. Conclusions and next steps

Given the benefits of PPFs for mobilizing resources and providing technical support to developing countries implementing PPPs, and based on the experience of IDB in leveraging its sectoral knowledge as well as its in-country presence in the Latin American and the Caribbean region to partner with countries to improve private-sector participation, it is clear that PPFs are a valuable instrument for IDB to support PPP. Therefore, PPFs should be a key component of IDB PPP strategy in the future.

Nevertheless, rather than standalone instruments, PPFs at IDB should be implemented as part of a comprehensive PPP Institutional framework that includes dedicated and trained staff, a sound PPP strategy that integrates our sectoral and country strategies and, finally, that works smoothly and efficiently with the different knowledge sectors.

## Annex 1

### Other PPF models in operation

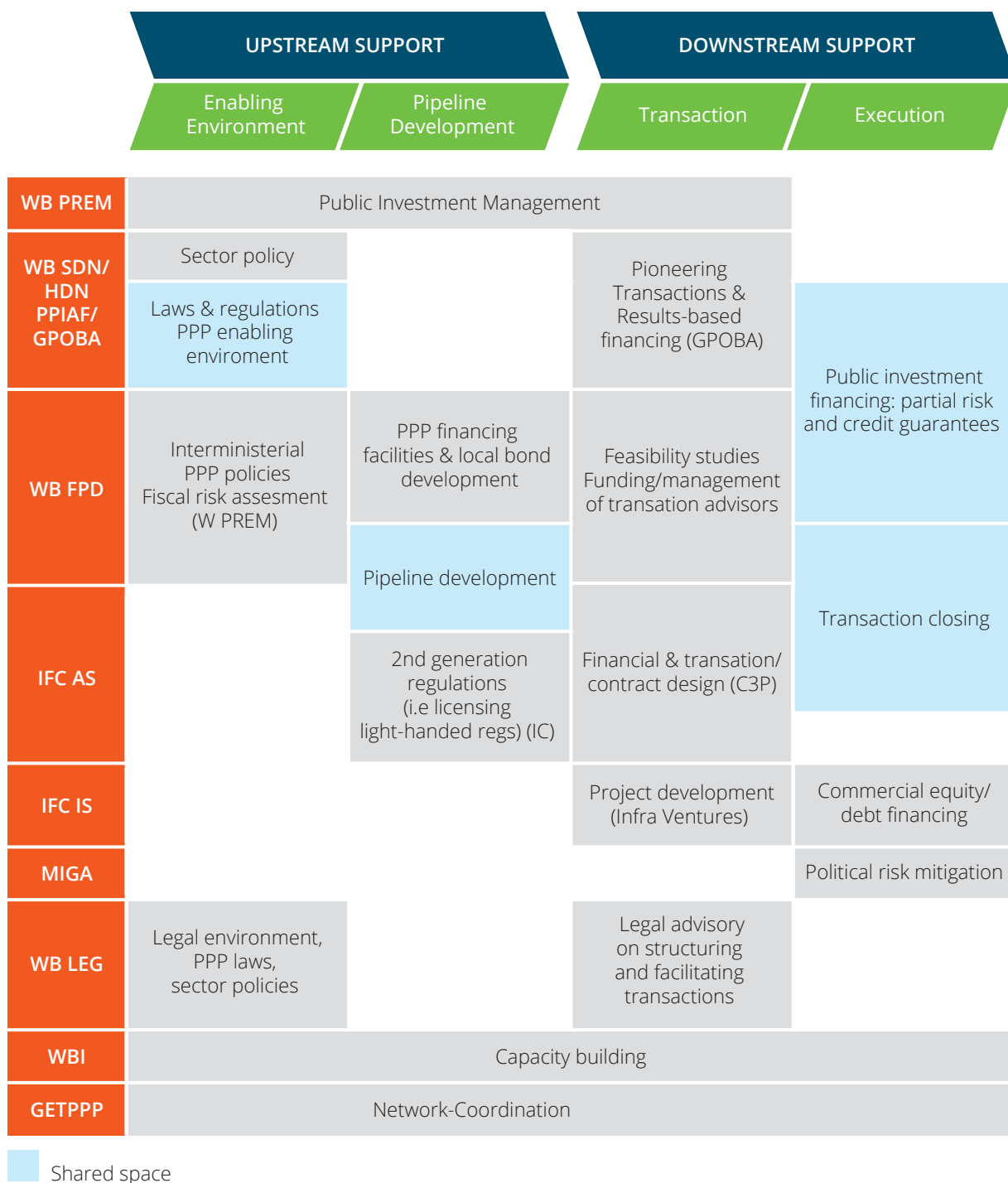
In addition to the PPFs, MDBs have structured a variety of other instruments and services to support PPP. Those instruments are in many ways complementary to the PPFs themselves, as in the case of the World Bank, or may cover some of the objectives shared by the PPFs, but are embedded in a different model, like the EIB's program known as Joint Assistance to Support Projects in European Regions (JASPERS).

### Support for PPP at the World Bank Group

The World Bank Group has deployed a wide range of instruments and services targeting PPPs during the period from 2002 to 2012. The World Bank's Independent Evaluation Group identified 165 IFC investments in PPP with total commitments of US\$6.1 billion, 71 MIGA guarantees issued in support of PPP projects with a total of US\$4.2 billion in gross exposure, and 157 IFC PPP Advisory Services with total funding of US\$187 million. On the public sector side, the International Bank for Reconstruction and Development (IBRD)/International Development Association (IDA) approved 203 lending and partial risk guarantee (PRG) projects during FY02-12 with a PPP component amounting to US\$23 billion, of which nine are PRG projects in total guarantee amount of US\$805 million; complemented by 120 capacity-building activities of the World Bank Institute (WBI) and 788 trust fund-supported advisory activities by the Public-Private Infrastructure Advisory Facility (PPIAF), with total expenditures amounting to US\$155 million. Over this 10-year period, the WBG's support to PPPs has increased fourfold.

The WBG's support addressed issues along the entire PPP delivery chain, from upstream support for the enabling environment and pipeline development to downstream transactions and execution.

**Figure – World Bank Group’s Engagement along the PPP**



Overall, World Bank lending and PRG operations emphasize upstream work slightly over downstream support: 93% of all projects had an upstream component and 82% provided downstream support; most projects had both. In upstream work, the most common elements were capacity building (58%); policy, regulatory, and institutional reforms (48%); and sector reform and strategy (46%). The most common downstream component was

support to specific financing of transactions (49%). Transaction support without financing was seen only in 10% of the PPP portfolio projects.

The Private Infrastructure Advisory Facility (PPIAF) supported 788 projects between FY02 and FY12, mainly supporting countries upstream in their PPP agenda. The WBI aided through capacity building at all stages of the PPP project cycle. The IFC invested in 165 investment projects that have been identified to support PPPs, amounting to US\$6.5 billion in commitments between FY02 and FY12. MIGA provided guarantees for 71 PPP projects that have been identified as supporting PPP, amounting to US\$5.2 billion between FY02 and FY12—nearly half of its total guarantee volume issued during this period

IFC Advisory Services under the PPP business line have increased significantly since FY05, supporting 157 services between FY05 and FY12. These 157 advisory services comprise about 11% of IFC's total advisory services funding. Total IFC funding for advisory services in PPPs has increased over time from US\$9.5 million in FY05 to US\$29 million in FY12.

## **Africa50<sup>31</sup>**

Africa50 was launched by the African Development Bank in 2015, as an autonomous entity, legally and financially independent from the Bank group.

Africa50 is an infrastructure investment platform that seeks to enhance commercially sustainable projects through the two principal activities of project development and project finance. Its first goal is making skilled legal, technical and financial experts available from an early project stage, sharing costs with member governments and developers, and recovering its funding at financial close or through a carried interest in the project. Its second goal is operating a business line through which Africa50 will offer a full suite of financing products to support the African infrastructure sector. Africa50 is designed as a “one-stop-shop” that provides a holistic solution to market failure.

With an initial target capitalization of US\$500 million (to be scaled up to at least US\$1 billion), Africa50 aims to attract a variety of investors, including African states, international financial institutions, pension funds, sovereign wealth funds and private sector entities.

## **European Investment Bank<sup>32</sup>**

JASPERS is a technical assistance partnership managed by the EIB and co-sponsored by the European Commission (DG Regional and Urban Policy) and the EBRD.

JASPERS focuses on large projects with total costs exceeding EUR 50 million for environmental projects and EUR 75 million for transport or other sectors. However, there is

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<sup>31</sup> Based on Africa 50 website: <http://www.africa50.com/>

<sup>32</sup> Based on EIB website: <http://www.eib.org/>

flexibility regarding the thresholds in the case of small countries or where projects serve as pilot actions to establish best practices.

Beneficiary countries in 2015 were: (i) 16 EU member states: Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, France, Greece, Hungary, Italy, Latvia, Lithuania, Malta, Poland, Romania, Slovakia and Slovenia; and (ii) three accession countries: The Former Yugoslav Republic of Macedonia, Montenegro and Serbia.

Since the start of operations in 2006, JASPERS has completed 1,012 assignments. Through December 31, 2015, a total of 467 JASPERS-assisted applications for funding of major projects have been approved by the European Commission, for a total investment cost of EUR 72.24 billion, of which EU grants amounted to EUR 43.31 billion.

Those who are not yet availing themselves of JASPERS may obtain it, subject to the agreement of JASPERS' Steering Committee.

JASPERS operates on the basis of country action plans prepared for each member state in cooperation with the concerned beneficiary state and the European Commission. A managing authority acts as a central coordinator for each country and can request assistance from JASPERS.

Project preparation support includes: (i) upstream project screening to assess a project's viability and suitability for EU grant funding; and (ii) project development from the pre-feasibility and feasibility stages to final grant application.

The pre-feasibility stage comprises: (i) comments and guidance on master plans; (ii) assistance in developing project concepts vis-à-vis EU regulations; and (iii) preparation of the ToR for the beneficiary to select consultants. The feasibility stage comprises: (i) a methodological review of the feasibility study and recommendations for adjustments; (ii) review of intermediate studies; and (iii) final deliverables and recommendations for improvement.

JASPERS' assistance is provided free of charge and member states are not obligated to use JASPERS. There is also no obligation for JASPERS beneficiaries to borrow from the EIB and EBRD, nor is there any obligation on the part of the EIB and the EBRD to lend to beneficiaries of JASPERS assistance.

The decision to provide an EU grant for a project prepared with assistance from JASPERS remains always the responsibility of the European Commission



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