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BRIDGING THE INFRASTRUCTURE GAP: ENGAGING THE PRIVATE SECTOR IN CRITICAL NATIONAL DEVELOPMENT

BENEFITS, RISKS AND KEY SUCCESS FACTORS

FOREWORD

The delivery of sound and reliable infrastructure – from roads and bridges to public utilities – is a fundamental driver of economic growth, and the demand for such services is expected to surge over the coming years. Unfortunately, the allocation of funds for infrastructure projects is insufficient to cope with this projected increase in demand.

An annual figure of almost US$2.7 trillion is being invested worldwide, each year, in infrastructure, which corresponds to just under 4% of global GDP. Despite this, the global funding gap is widening. An estimated annual spend of US$3.7 trillion would be needed to meet the growth in infrastructure demand. The US$1 trillion gap[1] represents a 27% shortfall in global infrastructure investments, highlighting an urgent need for new investment sources to be identified.

A possible solution, with significant potential, is to boost private-sector engagement in infrastructure development. Over the past decades, the contribution of the private sector to infrastructure investments has increased. While the involvement of private investors and operators in infrastructure comes with clear benefits, some obstacles still need to be overcome, to ensure the success of a public-private collaboration.

Some of the key success factors of privatisations, and public-private partnerships (PPPs) in general, are:

- Having a sound sector strategy and policy mix to serve as a basis for the collaboration
- Having a robust governance model and methodology to select the best-fit private enterprise
- Selecting a qualified private party that can deliver on its promises
- Establishing an effective regulator and regulations to safeguard both the interests of the private investor and the general public
- Adopting a transparent approach to build support with key stakeholders

This paper outlines the main benefits of private sector participation in infrastructure development, and presents the main factors that would ensure the success of collaborations between the public and private sectors.

1. WEF (2014) – "Strategic Infrastructure, Steps to Operate and Maintain Infrastructure Efficiently and Effectively"

1. THE IMPENDING INFRASTRUCTURE GAP

Telecommunication, transport, energy, and water systems are critical components of modern-day societies. They connect people, enhance their quality of life, and enable trade and business operations. By acknowledging the vital role public utilities play in our lives, the importance of sound infrastructure to economic development becomes self-evident. While the full impact of infrastructure on GDP still needs to be determined, most studies identify a positive correlation between the two variables.[2]

Although infrastructure certainly plays a key role today, it is expected to become an even greater catalyst for growth in the future, in line with the increasing demand for the benefits of airports, public transport, roads, and other amenities.

Demand for most utilities, and transport infrastructure, is expected to surge in the future. Maritime container traffic is forecast to quadruple by 2030, given a doubling of global GDP.[3] World energy consumption is expected to grow by 48% from 2012 to 2040, driven by strong economic growth in developing countries.[4] Additionally, mobile and fixed data-traffic are expected to grow at 45% and 20% per year, respectively, between 2015 and 2021.[5]

Addressing this increase in demand calls for significant commitments to infrastructure. One such development is China's One Belt One Road (OBOR) initiative. The plan involves building transport and energy infrastructure across more than 60 countries in Asia, Africa, and Europe.[6] Since its announcement in 2013, 47 Chinese state-owned enterprises have participated in more than 1,600 projects.[7] As part of OBOR, major roads and maritime project routes will need to be developed. One landmark project is the China-Pakistan corridor, which is worth an estimated US$46 billion.[8]

The case of air transport clearly shows the implications of an increase in demand for utilities and transport infrastructure. According to the International Air Transport Association (IATA), the number of air travellers is expected to grow from 3.8 billion to 7.2 billion between 2016 and 2035.[9] This represents a 90% increase in passenger traffic in less than 20 years. To cope with such a surge in demand, the supply of air-transport infrastructure will need to follow suit. New terminals and runways will need to be built and airports will need to enhance their operations, by improving their slot allocation and co-ordination practices.

2. World Bank (2011) – How Much Does Infrastructure Contribute to GDP Growth?
3. OECD (2012) – Strategic Transport Infrastructure Needs to 2030
4. EIA (2016) – International Energy Outlook 2016
5. Ericsson (2016) – Ericsson Mobility Report
6. Quartz (2017) – One Belt One Road
7. Fortune (2017) – China New Silk Road Investments Surprisingly Weak Before This Week's Summit
8. Reuters (2015) – China and Pakistan launch economic corridor plan worth $46 billion
9. IATA (2016) – IATA Forecasts Passenger Demand to Double Over 20 Years

Multiple factors are behind this expected surge in demand. In developing economies, the most important drivers are urbanisation, industrialisation, and population growth. More specifically:

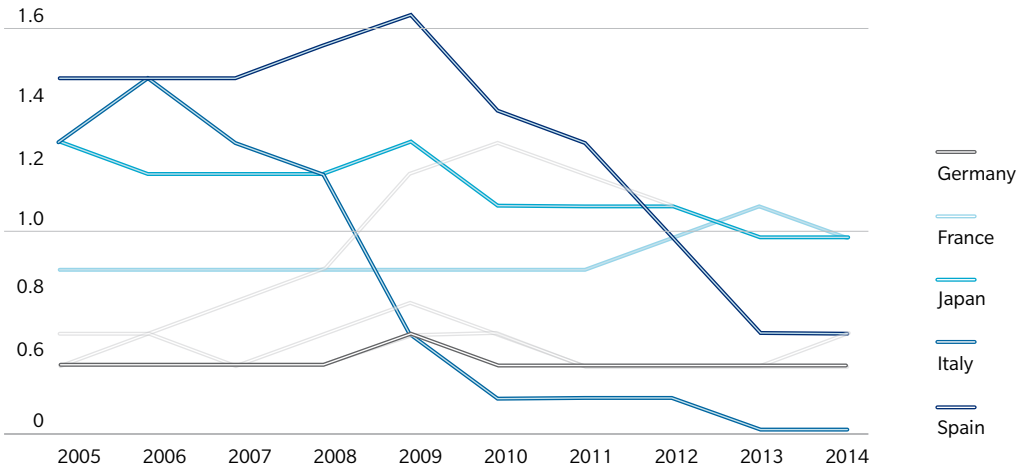
- The level of urbanisation in Africa and Asia is expected to grow by 40% and 33%, respectively, from 2014 to 2050. As a result, more than two thirds of the world's population is projected to be urban in 2050[10]
- With the highest rate of population growth among continents, Africa's population is expected to double within the next 30 years, accounting for more than half of the world's population growth between 2015 and 2050[11]

In developed economies, the main demand drivers are different, with the most important being the optimisation of legacy infrastructure. In the United States, for example, nearly 40% of bridges have been in operation for 50 years or more, and in 2016, 9% of them were considered to be structurally deficient.[12] Similarly, more than a third of Germany's rail bridges are more than 100 years old.[13]

Due to safety, environmental and performance concerns, developed economies need to invest in utilities and transport infrastructure to cope with new market conditions and requirements.

There are two challenges to meeting the increasing global demand for infrastructure. First, since the 2008 financial crisis, many governments have faced severe fiscal challenges and are hence cutting down on investments. Second, private investors are reluctant to commit capital to long-term, risky projects. As such, the bearish stance of the public and private sectors is limiting investments, as suggested by the overall drop in infrastructure investments across G7 nations between 2008 and 2014 (see Exhibit 1).[14]

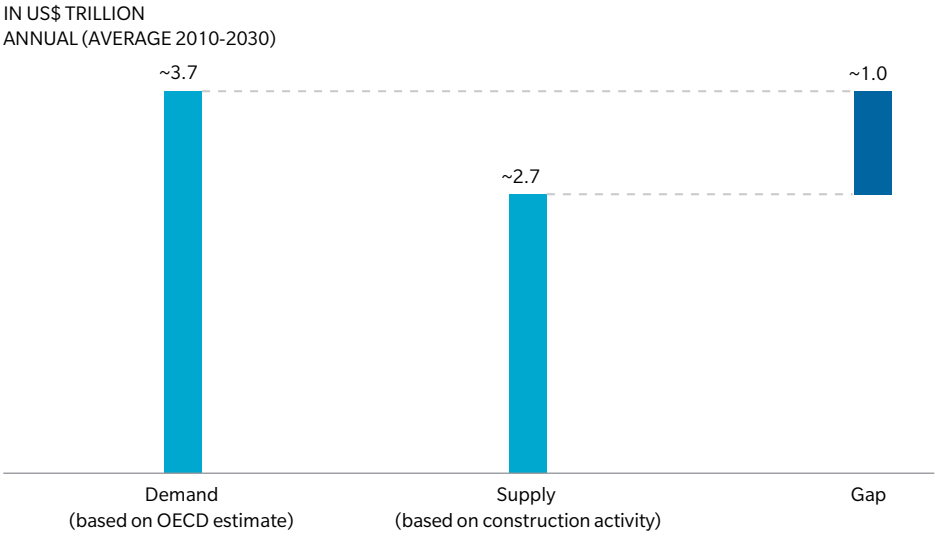
Exhibit 1: Infrastructure investment, Total inland investment as % of GDP



10. United Nations (2014) – World Urbanization Prospects, The 2014 Revision, Highlights
11. United Nations (2015) – World Population Prospects: The 2015 Revision
12. ASCE (2017) – Infrastructure Report Card
13. WEF (2014) – Strategic Infrastructure, Steps to Operate and Maintain Infrastructure Efficiently and Effectively
14. OECD (2012) – Strategic Transport Infrastructure Needs to 2030

Today, nearly US$2.7 trillion is being invested worldwide, each year, in infrastructure, which corresponds to almost 4% of global GDP. However, it has been estimated that an annual spend of US$3.7 trillion would be needed to meet the global growth in infrastructure demand. Hence, there is an annual gap in worldwide infrastructure investment of nearly US$1 trillion (see Exhibit 2),[15] or a 27% shortfall.

Exhibit 2: Overview of global infrastructure demand and supply



Considering the challenges that are hampering our ability to bridge the growing infrastructure gap, two possible solutions exist:

- Governments could reverse their current spending policies and resume their role as principal financiers of infrastructure projects
- Private investors could get more involved in infrastructure development

Given the current fiscal pressure felt by many governments, the first solution is unlikely to be optimal. As such, governments should find effective ways to incentivise and manage greater private-sector involvement in infrastructure.

Whereas more than 50% of infrastructure projects are privately funded in developed economies, private investments in emerging markets and developing economies (EMDEs) remain limited. Today, nearly 70% of infrastructure projects in EMDEs are financed by government budgets, 10% by multi-development banks, and the remaining 20% by private investors.[16]

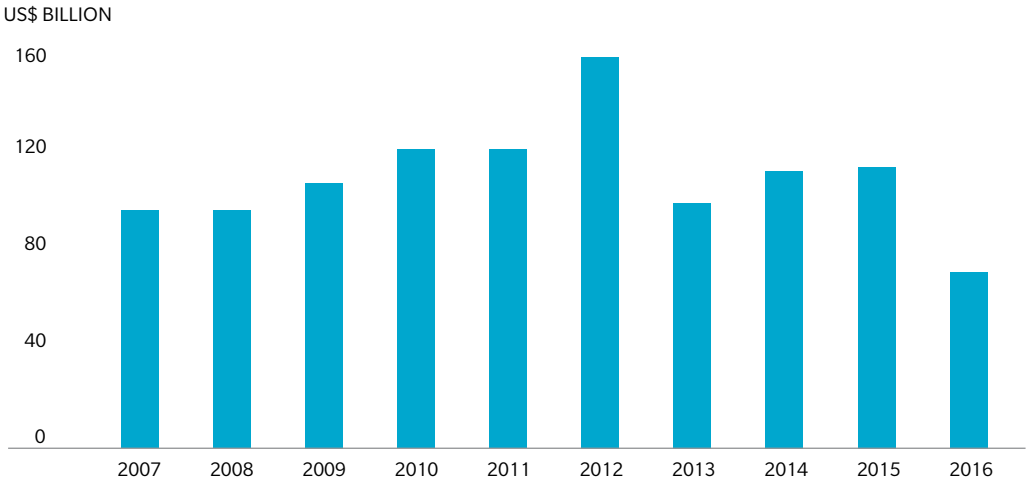
15. WEF (2014) – Strategic Infrastructure, Steps to Operate and Maintain Infrastructure Efficiently and Effectively

16. Oliver Wyman (2017) – Closing the Financing Gap

Looking at private investment levels across EMDEs over the past 10 years, these markets do not seem to be attractive enough. Despite a peak of US$160 billion in 2012, investment commitments in 2016 were just US$72 billion, well below the US$95 billion in 2007 (see Exhibit 3).[17] Therefore, the governments of developing economies should work on enhancing the attractiveness of infrastructure opportunities.

An example of this is the One Belt, One Road (OBOR) initiative, estimated to be worth US$1.3 trillion. Over the next five years, it is expected that investments worth around US$300-500 billion will be channelled into OBOR-participating countries.[18] Despite the anticipated economic development, financing OBOR will be challenging. Its success depends on the private-sector participation of banks, funds, and corporations. In recent years, China has committed to dispensing approximately US$113 billion in funding, through various channels, including the China Development Bank and the Silk Road Fund. Multilateral institutions such as the Asia Infrastructure Investment Bank (AIIB) and the New Development Bank will be essential financers of the initiative. AIIB has already approved US$1.7 billion in loans for nine OBOR projects. Despite these commitments, there is still an investment shortfall, and the private sector is the likeliest candidate to address it.

Exhibit 3: Investment commitments in infrastructure with private participation in EMDEs, 2015



Note: All investment is adjusted by US CPI
Source: PPI Database, World Bank, as of June 2017

In the Middle East, most attempts to drive greater private engagement in infrastructure have failed. During the 1990s, following a prolonged period of low oil prices, GCC governments sought to diversify their economies and reduce their dependence on petrochemical revenues. Increased private-sector participation was viewed as a potential solution. In fact, in 1994, the governments of both Oman and Saudi Arabia included privatisation goals in their short- and mid-term development plans. Yet nothing happened.

17. World Bank (2016) – Private Participation in Infrastructure, Annual Update
18. Bloomberg (2017) – Top Miner Sees "Huge Demand" Boost from China's New Silk Road

Why? First, GCC governments lacked the motivation to increase private-sector involvement. Indeed, the moment oil prices grew past the fiscal break-even point, the pressure to reform dissipated, and most plans to involve the private sector in public utilities were dropped. Second, a number of previous, high-profile attempts had proved unsuccessful, discouraging further efforts and accentuating the general public's fear of the loss of control over the provision of utilities.

Looking deeper, four primary obstacles can be identified that prevented GCC governments from achieving their privatisation and PPP objectives (see Exhibit 4).

Exhibit 4: Major obstacles to private sector participation in the GCC

1	**LACK OF SUSTAINED POLITICAL WILL**	• Government agendas change due to different circumstances or new key players • Institutional prerequisites are not implemented in due time and hence stall progress
2	**SIZE OF PUBLIC SECTOR WORKFORCE**	• Labour market might not be able to absorb redundant workers • Resistance from labour force can be significant
3	**CAPACITY AND ROLE OF PRIVATE SECTOR**	• Domestic private sector is not prepared and lacks experience for major investments • Foreign ownership rights insufficiently assured and foreign investments too strictly regulated
4	**BUREAUCRACY, RED TAPE AND GOVERNMENT RESISTANCE**	• Conflicting agendas in the government hinder progress • Lack of experience with regulatory tasks vis-à-vis control over operations

Governments can no longer rely on public funds to meet the growing demand for public utilities. The private sector needs to be involved. Failing to meet the global infrastructure demand means missing out on a significant economic opportunity. Assuming a 10% elasticity of GDP to infrastructure capital,[19] and a total demand for infrastructure investments worth US$3.7 trillion annually, closing the annual US$1 trillion gap could lead to an increase in global GDP of almost 4% per year. In 2017, this would represent nearly a US$3 trillion increase in global GDP. Considering such a growth in GDP is non-negligible, governments should find ways to incentivise and better handle public-private collaborations.

Private-sector involvement brings benefits, but it also presents challenges, and it is to these, as well as to key factors in making such collaborations succeed, that this paper now turns.

19. World Bank (2011) – Is Infrastructure Capital Productive? A Dynamic Heterogeneous Approach

2. THE UPSIDES OF PRIVATE-SECTOR INVOLVEMENT

There are three main ways to involve the private sector in public utilities. Private actors could:

1. Oversee and manage the operations of public infrastructure for a limited time period;
2. Support the government with greenfield infrastructure projects, handling both the construction and management of the asset;
3. Become the owner(s) of public infrastructure

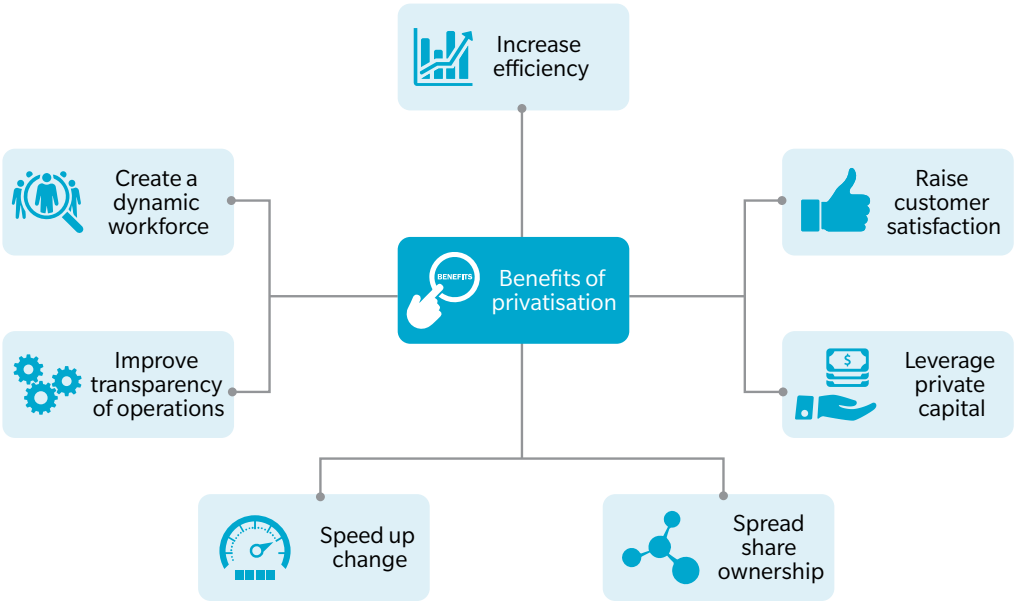
The responsibilities and requirements of the private party change, depending on the type of collaboration (see Exhibit 5).

Exhibit 5: Types of public-private collaborations

	Ownership	Operation	Capital Investment	Duration
PUBLIC AGENCY	Public	Public	Public	N/A
SERVICE CONTRACT	Public	Public/Private	Public	1-2 years
MANAGEMENT CONTRACT	Public	Private	Public	3-5 years
LEASING CONTRACT	Public	Private	Public/private	5-15 years
CONCESSION	Public	Private	Private	15-30 years
BUILD, OPERATE, TRANSFER	Public/Private	Private	Private	15-30 years
PRIVATISATION	Private	Private	Private	Indefinite

Exhibit 6 illustrates the benefits of private-sector participation and highlights how it offers financial, social and economic benefits that help governments meet the needs of their people. Considering infrastructure projects in particular, the two main benefits from greater private-sector participation are improved performance and increased access to capital.

Exhibit 6: Benefits of private-sector participation



IMPROVED PERFORMANCE

The majority of publicly owned and operated utilities deliver sub-par performances. In most cases, a combination of technical, institutional, and financial issues result in poor cost recovery and unsatisfactory, unreliable services. Kuwait International Airport, for example, was subject to severe criticism in 2016. That year, on peak days, waiting times reached up to 3.5 hours, leading to delays in more than 50% of flights, which left passengers disgruntled.

The private sector's involvement can resolve some of the operational issues of public utilities. By leveraging their technical expertise, and by delivering greater value through innovation, private companies can enhance the performance of public infrastructure.

To measure the potential effect of the private sector on the performance of public utilities, the World Bank conducted a study on 1,200 water and energy utilities in 71 developing and transition economies.[20] The study found strong evidence for the positive impact of private participation. Private operators managed to expand coverage, increasing the average number of residential water connections by 12%. They also improved service quality and efficiency, with an 11% reduction in electricity losses and a 41% increase in electricity supply per day.

INCREASED ACCESS TO PRIVATE CAPITAL

Given the current tight monetary policies employed by most governments, the private sector can help ease the pressure on public finances by providing the capital required to build and expand infrastructure. In 2016 for example, the private sector committed more than US$70 billion in infrastructure projects in emerging markets and developing economies (see Exhibit 7). Additionally, in most cases, private bodies tend to allocate funds more effectively. The IMF estimates that, across countries, about one third of public investment is lost, through a combination of waste, corruption and bad management.[21]

Exhibit 7: Investment commitments in, and number of infrastructure projects with, private participation in EMDEs in 2016

	Number of transactions	Total investment US$ billion	% Total
ENERGY	162	43.8	61.4
TRANSPORT	53	25.7	36.0
WATER AND SEWERAGE	27	1.9	2.6
TOTAL	**242**	**71.4**	**100**

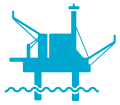
Source: PPI Database, World Bank, as of June 2017

It is also interesting to note that these two benefits complement and reinforce one another. For example, greater efficiency leads to cost savings that allow for more funds to be re-invested into the asset. But also, improved management and performance result in easier access to private capital.

20. World Bank (2014) – Does Private Sector Participation Improve Performance in Electricity and Water Distribution?
21. IMF (2016) – Remarks for Conference on Meeting Asia's Rebalance and Growth Challenge

Over the past decades, private companies have showcased the value the private sector can bring to infrastructure (see Exhibit 8).

Exhibit 8: Successful public-private collaborations in infrastructure

Sector	Country	Asset	Involvement	Major Impact
Airport 	**Jordan**	Queen Alia Int'l Airport	25-year concession	• Tripling of capacity • 45% increase in daily traffic • Greater profitability and more than $1 billion in foreign investment
	Denmark	Copenhagen Airport	60% sale to private sector	• Passenger satisfaction consistently above 85% • Named by IATA, most efficient airport in Europe for 11 years
Seaport 	**Madagascar**	Toamasina Port	20-year concession	• Tripling of container movement per hour • Halving of average clearance time • Cancellation of port surcharge
	Brazil	Suape Container Terminal	30-year BOT	• 500% increase in port handling activity • 140% increase in port employment
Power Generation 	**Oman**	Four plants	Sales of plants – Accounting for 70% of national electricity production	• 164% increase in supply • 75% growth in customers

3. THE POTENTIAL PITFALLS OF PRIVATE SECTOR INVOLVEMENT

While the potential benefits from private sector participation are clear, there are often significant obstacles to overcome. In the past, many privatisation and public-private partnership attempts have failed, due to the government's inability to recognise and counter the potential risks from increased private-sector involvement (see Exhibit 9).

Exhibit 9: Failed public-private collaborations and main failure drivers

Country	Asset	Unqualified private actor	Lack of pol. commitment	Overstaffing in public sect.	No clarity on expectations	Poor reg. framework
OMAN	Salaleh Airport and Seeb Int'l Airport				X	X
MEXICO	Toll roads (5,000 km)	X			X	
INDIA	Ennore Port Container Terminal	X			X	X
BOLIVIA	Cochabamba Water Supply and Sanitation	X			X	X
KSA	Saline Water Conversion Co. and Saudi Electricity Co.		X	X		X

There are five major risks that can lead to the failure of collaborations between the private and public sectors.

UNQUALIFIED PRIVATE-SECTOR ACTOR

A factor that might result in a project's failure is the selection of the wrong private investor. In general, deep industry expertise, though necessary, is not sufficient. The private party should also have a clear understanding of the market of the target infrastructure or asset, to determine the best approach in both winning the local population's approval and developing a reliable business plan. Social backlash and unaccounted-for market changes, such as currency fluctuations, can be fatal to a project. This is especially true for infrastructure development projects, given that they are capital intensive, and have long gestation, and even longer payback, periods.

LACK OF SUSTAINED POLITICAL COMMITMENT

Given the complex nature of infrastructure projects, substantial political commitment is required, particularly when aligning the interests of numerous stakeholders. Yet sustaining such commitment can prove challenging over the longer term, because many of the political costs of public-private partnerships and privatisations are often incurred in the short term, whereas benefits are usually reaped in the long-term. For example, labour and operational restructuring activities occur long before productivity and service quality benefits can be perceived. This is all the more true in cases where such benefits are accrued only after the point when the concerned ministers have left office.

OVERSTAFFING IN PUBLIC-SECTOR LABOUR FORCE

In many countries, including those within the GCC, the public sector is the primary employer of the local labour force. Nationals employed in the public sector also enjoy high wages and job security. These entities are, in effect, often acting as a substitute for a welfare state.

Given the profit-seeking nature of private companies, increased efficiency often implies a reduction of the entity's workforce, which leads to two major problems. First, it can result in resistance from workers who risk losing their jobs. Second, it can have a negative effect on employment overall and, by extension, on economic output, if other sectors of the economy are not able to absorb workers who have been made redundant. Accordingly, privatisations and PPP initiatives must overcome any short-term effects on labour and output if they are to be successful.

NO CLARITY ON EXPECTATIONS AND POOR AGREEMENT DESIGN

Before a public-private collaboration can occur, the government needs to have a clear view on the general direction of the sector in which the infrastructure will operate. For example, when it comes to the telecommunications sector, the government should define an ICT strategy and set coverage and service-quality targets. Such goals need to be incorporated into the terms of public-private collaboration. The government needs to make sure the targets allow the project to remain economically viable for the private participant, while maintaining overall social welfare. Failing to set sector targets limits a government's ability to monitor the private company and hold it accountable for its actions.

POOR REGULATORY FRAMEWORK AND ENVIRONMENT

Excessive red-tape can unnecessarily burden private companies. However, too little regulation can lead to anti-growth outcomes and ultimately harm the general public. A sound and balanced regulatory framework is thus vital to the success of public-private collaborations.

Having proper regulation is critical when it comes to large infrastructures, which are often natural monopolies. Since there is little room for competition, the private operator may not be compelled to enhance the efficiency of the business or ensure high-quality outputs. In the case of developing nations, this risk is even greater. To generate greater profits, private operators may disregard the interests of lower-income citizens. In such markets, the regulator plays a critical role in ensuring collective interests are not neglected. Effective oversight requires the establishment of rules on tariff control, quality and environmental safety.

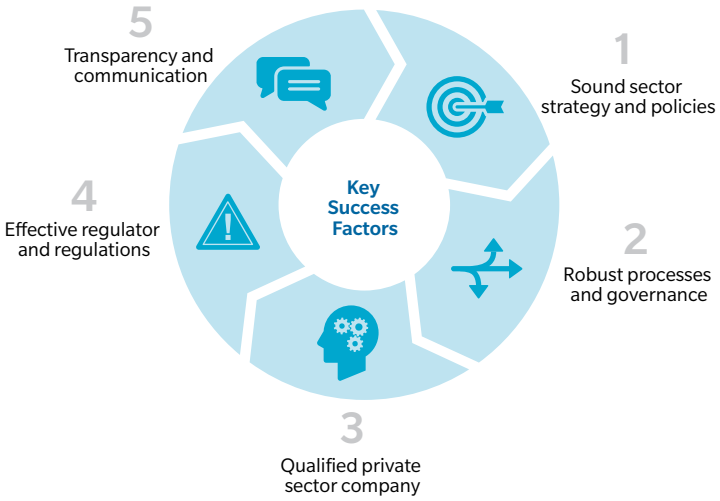
Beyond strong regulation, the government needs to ensure the regulator is able to enforce policies, and guarantee the compliance of private companies with sector guidelines. The inability of regulators to monitor and control the activities of private operators can lead to abuses, such as price hikes and deteriorated service quality, undermining overall welfare.

In the GCC, a major issue is the lack of, or poor performance of, regulators. Many regulatory authorities are not mandated to enforce policies or have yet to be made fully operational. Another issue is the lack of operational independence of regulators, due to their dual role as market participant and regulator. In one case, a regulator that was responsible for both operating a facility and for setting the prices for its use, set charges that were above the socially optimal level.

4. HOW TO ENSURE SUCCESS

Based on these challenges and the leveraging of international best practices, five key success factors for private sector participation in infrastructure have been identified (see Exhibit 10).

Exhibit 10: Key success factors for private sector participation in infrastructure



SOUND SECTOR STRATEGY AND POLICIES TO SERVE AS BASIS FOR COLLABORATION

Before involving the private sector, it is crucial for governments to set clear sector targets. For example, the target number of households to be connected to a given public utility, and the quality of outputs in the mid- and long-term, should be determined. Based on these overarching objectives, the government then needs to identify and select projects from a pool of greenfield and brownfield candidates, accounting for its fiscal and time constraints.

The UK government, for example, has defined clear guidelines for the transport sector. In 2006, the government released a study on the current state of this industry and defined principles to guide the development of transport policies. One such recommendation was to focus on the rehabilitation of current infrastructure, rather than new construction.[22] Additionally, based on its long-term goals and capacity, the government developed a transport investment strategy, highlighting the types of projects it would undertake and support to ensure the UK meets its infrastructure needs.[23]

22. UK Gov. (2006) – Eddington Transport Study
23. UK Gov. (2006) – Eddington Transport Study

Once prospective projects have been identified, policy-makers then need to set guidelines that safeguard both the interests of the private investors and those of the general public. Successful policies protect consumer rights, while ensuring that regulations are economically sound. These policies should also serve to alleviate the fears of key stakeholders. For example, rules on the protection of public-sector employees and the restriction of foreign control over public utilities should be developed.

ROBUST GOVERNANCE MODEL AND PROCESSES TO SELECT OPTIMAL PRIVATE INVESTOR

The government must define clear guidelines and procedures for the selection of private investors. A common practice, with clear benefits, involves the development of framework legislation (e.g. prioritisation of assets, bidding processes, ways of selecting finalists, etc.). Doing so improves the transparency, consistency and effectiveness of the process, generating greater confidence in potential investors. As such, adopting framework legislation can increase the number and quality of prospective investors.

The government should also create a central body to drive the private investment programme. This governance model carries two major benefits. First, the central authority would be able to co-ordinate private-sector participation efforts across all sectors. Second, privatisations are highly complex processes, involving more than 130 major steps, which sometimes require specific expertise in finance, law or HR. Such steps would need to be conducted by specialised firms. Considering privatisations can take up to five years, it is crucial to have a central authority to oversee and co-ordinate the work of the specialised firms and various government agencies.

QUALIFIED PRIVATE SECTOR COMPANY THAT WILL EXECUTE ON ITS PROMISE

Beyond the lack of required capabilities, numerous private companies have failed, in the past, to abide by the terms of their agreements, due to poor business planning:

- Forecast revenues were too optimistic against actual income, leading to bankruptcy of private investor
- Market risks were disregarded, such as changes in currency and political instability
- Local culture was poorly acknowledged, resulting in low acceptance rate of private-sector involvement, and increased social backlash

Therefore, before entering into long-term contracts with private parties, governments need to make sure the selected private party has the right expertise and capabilities, but also that its business plan is economically sound.

In the air-transport sector, major airport operators, such as AENA and Aeroport de Paris, have significantly increased their global footprint. By building both their technical expertise and their socio-cultural understanding of different geographies and markets, they have proven to be valuable private partners.

EFFECTIVE REGULATOR AND REGULATION TO PROTECT GENERAL PUBLIC AND INVESTOR'S INTERESTS

Given the high-risk profile of infrastructure projects, governments need to account for the profit-seeking nature of private companies. Although they should prevent monopoly profits, governments should not set artificial limits on the investor's earnings based on populist demands. Otherwise, major incentives from increased private-sector involvement, such as greater investment, efficiency, and innovation, would be undermined. As such, when setting sector regulations, it is crucial to find the right balance between the interests of private investors and those of the general public.

Looking at the example of seaports, the best regulatory frameworks push for port tariffs that are high enough to ensure the economic viability of the private operator, but low enough to prevent the artificial inflation of the price of goods entering the country.[24] Beyond price caps, regulations on the quality and safety of services provided should be set. These guidelines will help reduce congestion issues and avoid damage to cargos, which ultimately leads to higher port charges that are transferred to consumers. Such regulation prevents private operators from focusing solely on expensive cargo, which would lead to hikes in the costs of less expensive shipments, due to higher waiting times.

Though effective regulation is crucial, it is not sufficient to properly control the workings of the private sector. Having a strong regulator that can effectively monitor and enforce regulatory requirements is equally critical.

Another important issue arises where a government serves as both the economic and safety regulator, and the operator. Having the government retain a substantial stake in the privatised entity may provide some comfort to investors that regulations will be reasonable, but a far better approach is to separate the government's regulatory responsibilities from any role in seaport operations.

TRANSPARENCY AND COMMUNICATION WITH KEY STAKEHOLDERS TO BUILD SUPPORT

Transparency and regular and effective communication are fundamental to the success of private-public collaborations. Failure to ensure transparency has several drawbacks:

- Reduction of investors' willingness (specifically foreign investors) to bid for public infrastructure
- Increased likelihoods of corruption and selecting an inadequate investor
- Reduction of overall public acceptance of the process, potentially leading to social backlashes and protests
- Increased ambiguity regarding the expected outcomes of the collaboration, which negatively affects the policy, and generates uncertainty in the market

24. World Bank (2000) – Privatization and Regulation of Transport Infrastructure: Guidelines for Policymakers and Regulators

One possible solution is to have the programme regularly monitored and audited by a well-financed, independent agency reporting to a parliament or similar authority. Additionally, the entity in charge of the project should involve key stakeholders, such as unions, asset tenants, government agencies, and even the general public, to gain their support and approval.

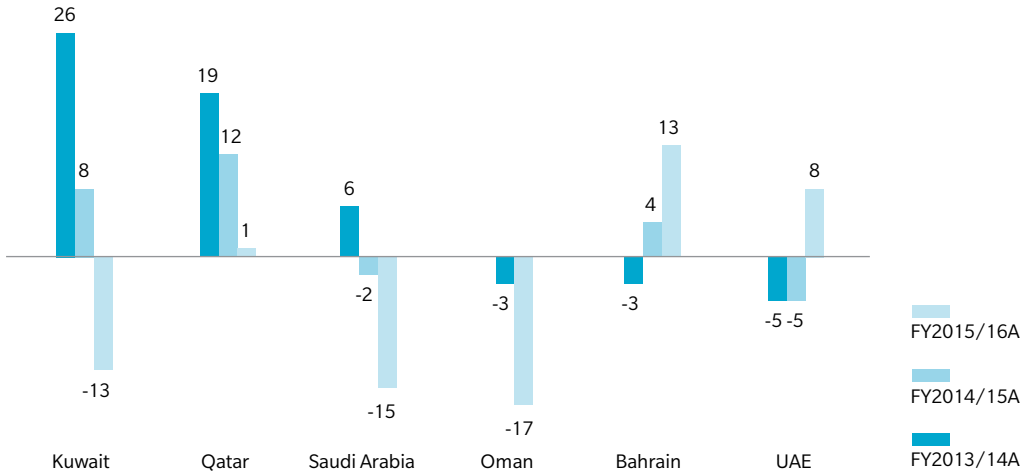
To ensure transparency, the French government, for example, included formal procedures for the consultation and collaboration of citizens in the preparation of infrastructure projects. Legislation adopted in 2002 requires the involvement of citizens, through public discussions and debates, from the initiation of the preliminary design studies until completion of the public inquiry. The public must also be kept fully informed during the construction stage, until the final entry into service of the infrastructure.[25]

25. OECD (2005) – National Systems of Transport Infrastructure Planning

5. WHY NOW FOR THE GCC?

The drop in oil prices, from a peak of US$115 per barrel in June 2014 to under US$35 in February 2016, has left GCC countries struggling to adapt to a new economic reality. Considering that oil accounts for the majority of national revenues, the depreciation in the value of fossil-fuels has had a deep impact on the fiscal balances of Arab Gulf countries.[26] In Saudi Arabia, for example, 2015/16 deficits reached over US$95 billion, or 15% of GDP (see Exhibit 11).

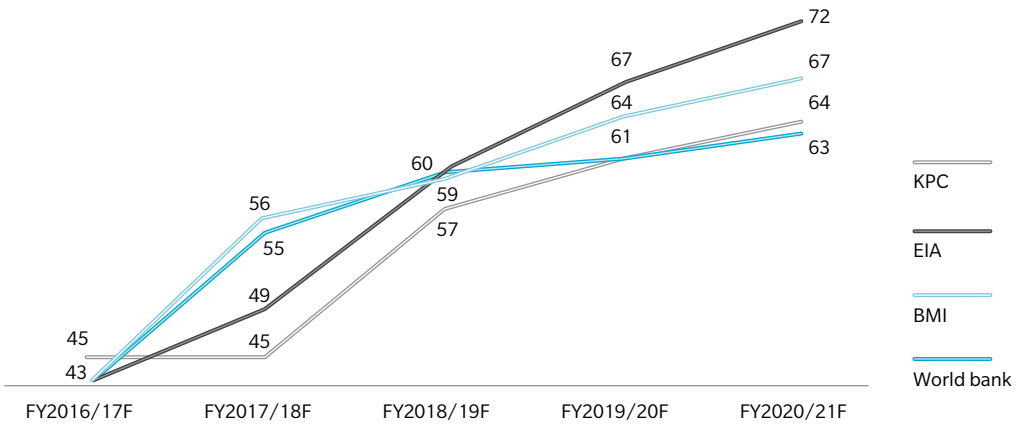
Exhibit 11: Fiscal balances in GCC countries around the oil price shock (% GDP)



26. Oxford Economics

Given the current forecasts of oil prices over the next five years (see Exhibit 12), the current run-rate of public spending and revenue of GCC governments is unsustainable. In a status-quo scenario, Kuwait's fiscal deficit, for example, would continue to increase with a potential cumulative shortfall of around US$87 billion by the end of fiscal year 2020/21.[27]

Exhibit 12: Oil price forecast (US$ per barrel), as of March 2017



With future deficits looming, GCC countries have decided to pursue economic and fiscal reform programmes. Today, these countries should make the most out of their current situation, to transform their economies, making them more balanced and sustainable.

Robust economies rely on a dynamic private sector. As such, GCC governments should favour private-sector involvement over the coming years. In particular, GCC countries should benefit from the private sector's ability to inject capital and improve the performance of major infrastructure.

WHAT SHOULD GCC GOVERNMENTS DO TO SUCCESSFULLY INCLUDE THE PRIVATE SECTOR?

A main take-away from international experiences is that preparation is vital to effective execution. As such, GCC governments should lay the groundwork for increased public-private collaborations, focusing in particular on four main activities (see Exhibit 13).

27. Kuwait Ministry of Finance, including transfer to Kuwait's Future Generation Fund

Exhibit 13: Recommended preparatory actions

1. Define clear objectives for increased private sector involvement

The government should develop concrete private sector involvement objectives that will serve as a basis for its privatisation and public-private partnership programme. Every country presents a unique combination of economic, political and socio-cultural features. As such, countries might have different fiscal, economic and social objectives (see Exhibit 14). In the GCC, although some governments have already defined privatisation objectives, they should re-evaluate them to reflect the dramatic change in their macro-economic landscape.

Exhibit 14: Privatisation programme objectives

			Kuwait	Saudi Arabia	United Kingdom
1	FISCAL	Reduce debt burden	✓		
		Collect tax and concessions revenues		✓	✓
		Reduce operating expenditures/subsidies	✓	✓	
2	ECONOMIC	Build competitive markets	✓	✓	✓
		Improve operational efficiency	✓	✓	✓
		Stimulate innovation/bring know-how	✓		
		Develop capital markets	✓	✓	✓
3	SOCIAL	Create job opportunities		✓	
		Enhance service levels and pricing		✓	✓
		Build an ownership culture	✓	✓	✓

2. Set up an effective central authority to oversee the programme

As highlighted previously, governments should establish an independent central authority to manage privatisation and PPP processes. This entity should oversee the process from the initial selection of assets to privatise to the transfer of management or ownership of public infrastructure. Given the limited privatisation history of the GCC, concentrating responsibility for privatisation planning and execution in a central agency would accelerate programme development.

In Jordan, the Privatization Law laid the groundwork for the establishment of a central authority, the Executive Privatization Commission (EPC), to run the country's privatisation programme. The law also empowered the EPC, allowing it to retain external advisors, undertake investor search and negotiate privatisation transactions. Being the sole agency in charge of privatisation, the EPC was able to build in-house capacity and institutional memory on the operations and procedures involved in planning and executing a successful privatisation.[28]

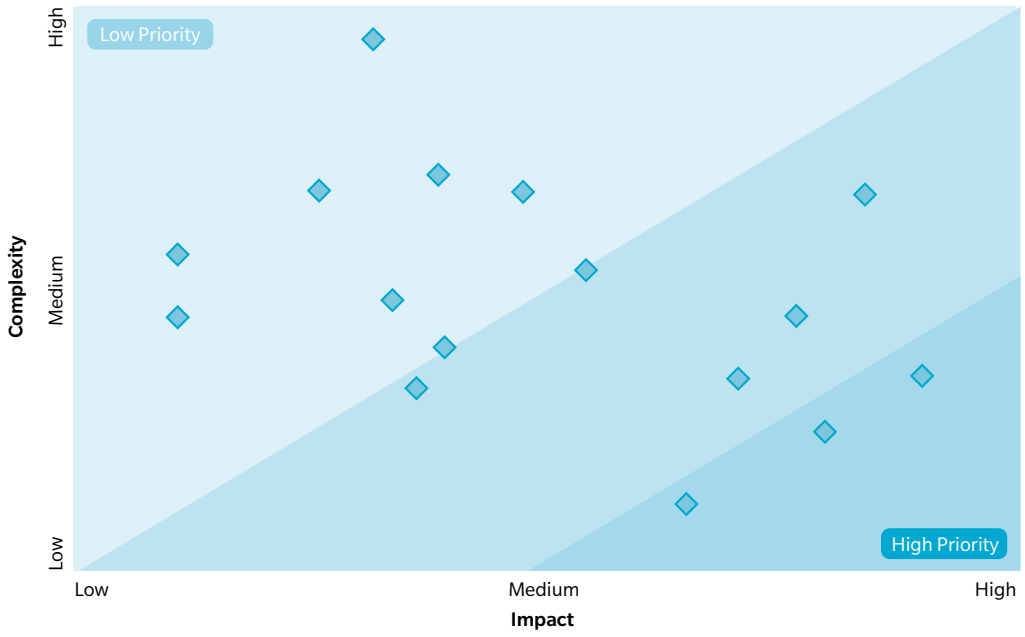
3. Develop clear and transparent procedures

Given the high-complexity of privatisations and public-private partnerships, as well as the unique nature of each country, having clear process guidelines is necessary. Legislation on the mandate and responsibilities of the central authority needs to be developed. Additionally, a detailed and comprehensive process guide, highlighting timelines, interdependencies and stakeholders, should be prepared to ensure the smooth execution of the plan and give comfort to prospective investors. Oliver Wyman developed one such process guide for a GCC government enabling it to properly plan and run its privatisation programme.

4. Develop the plan

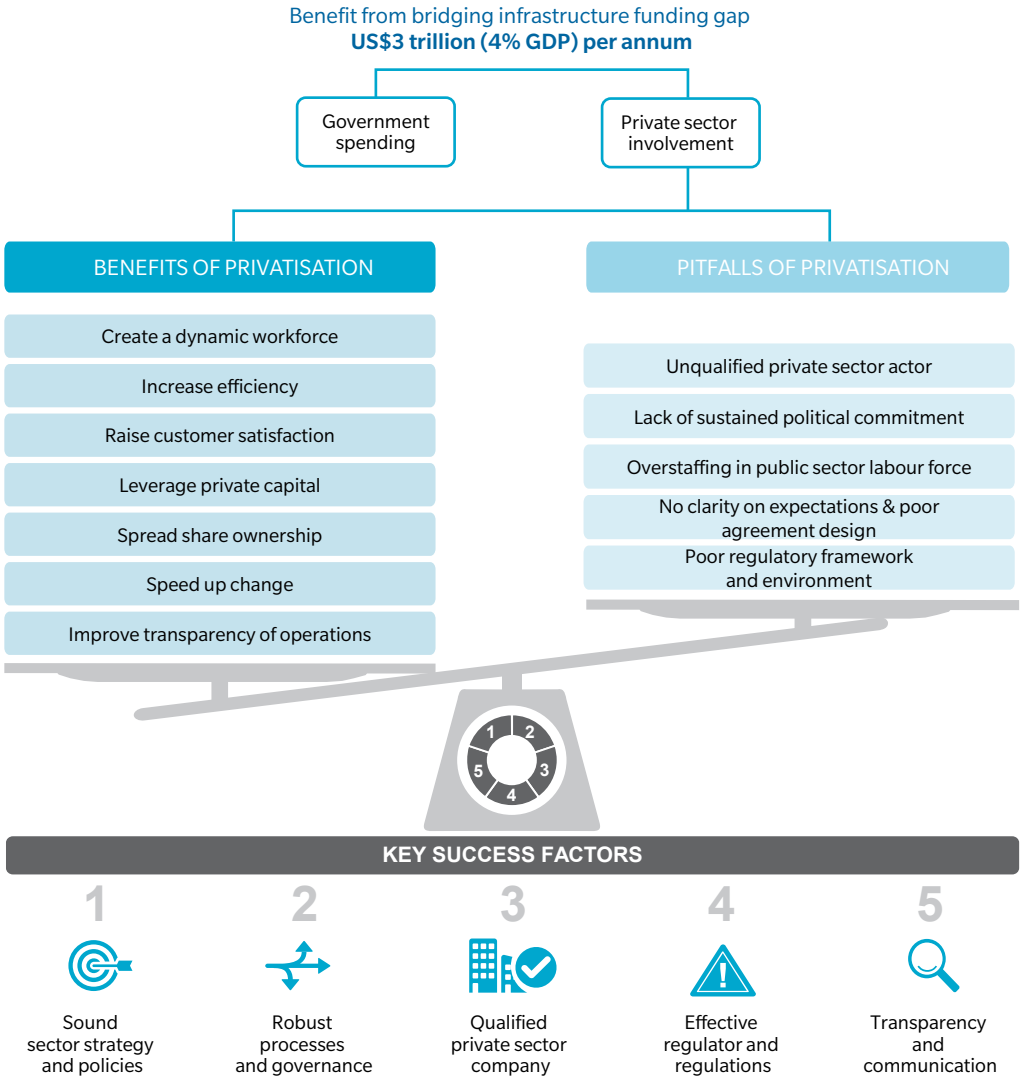
Before launching any specific privatisation, the central authority should identify and compare a range of possible opportunities for greater private-sector involvement. It should then prioritise these opportunities, by evaluating their overall complexity and potential impact against set objectives (see Exhibit 15). Once potential opportunities have been prioritised, the authority should prepare an implementation roadmap, accounting for its capacity (budget, human resources and technical capabilities).

Exhibit 15: Impact/complexity matrix



28. World Bank (2012) – Privatization: Lessons from Jordan

6. SUMMARY INFOGRAPHIC



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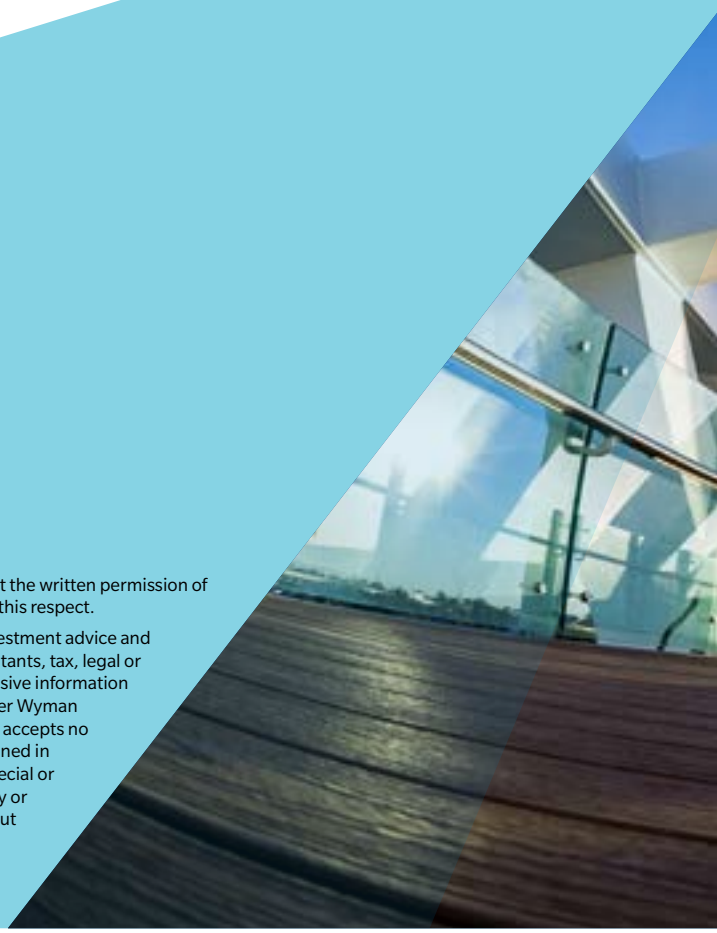

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