



***Gulf One***  
*Investment Bank*

**Research Bulletin**  
**July 2012**

**Public Private Partnerships in the GCC Region:  
What Went Wrong?**

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## Overview

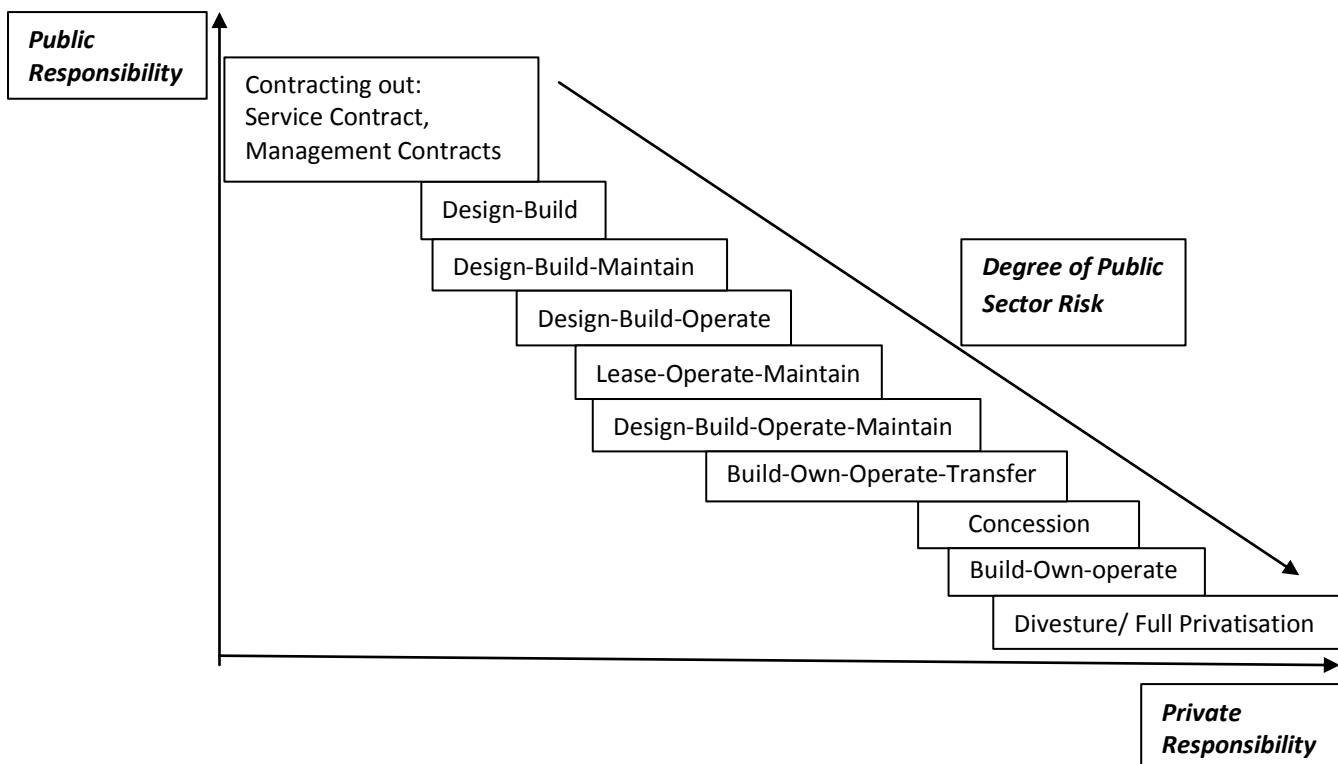
At the dawn of the new Millennium, there were cheerful and exciting comments about the flourishing potential of public private partnerships (PPPs) as an innovative mechanism for financing projects in the Gulf Cooperation Council (GCC) countries. The quest for PPPs in the region largely emanates from the huge investment requirements that currently exist in financing key infrastructure projects in many sectors such as water, power, transport, telecommunication, education, and healthcare. Despite the abundance of hydrocarbon resources, which have generated substantial amounts of windfall to the government coffers, the infrastructure financing gap in the GCC region is huge, estimated at US\$1.5 trillion over the next ten years, and the public sector alone cannot fully satisfy the growing demands for various infrastructure facilities and services. Neither could the private sector perform such a herculean task alone, hence the attractiveness of PPPs as an appropriate mechanism for financing mega infrastructure projects in the region.

In spite of the compelling need for PPPs, the appetite for such a financing mechanism has waned in the GCC resulting in recent years leading to suspension or cancellation of a number of projects. Two high profile PPP projects that were recently cancelled are the Landbridge railway project in Saudi Arabia and the Mafrag-Ghweifat road project in the United Arab Emirates. Both projects are now being executed solely by the public sector through engineering, procurement and construction (EPC). The cancellation of these and other PPP projects has cast doubts on the future of PPPs in the region, and the key questions are: what are the real reasons behind the waning of appetite on PPPs in the GCC region? What are the key obstacles or challenges facing PPPs in the region? What can be done to address those challenges in a bid to rekindle interest in such an innovative financing mechanism? What lessons could the GCC countries learn from the rest of the world? In the absence of PPPs, what other options can countries in the region pursue to accelerate infrastructure development that is needed to facilitate economic diversification, create jobs, boost income, and promote long-term prosperity and industrial development? This research bulletin seeks to provide answers to these and related questions.

## Nature and Extent of Public Private Partnerships

A public private partnership (PPP) has many connotations, but it can be broadly defined as “legal agreements between government and private sector entities for the purpose of providing public infrastructure, community facilities, and related services”<sup>1</sup>. As a result, the partners share responsibility, reward and risk associated with the joint investment. For example, the public sector’s contribution to a PPP may take the form of capital for investment or in-kind contributions, and the government can also mobilise political support for the project and provide assistance on environmental awareness, local knowledge, and social responsibility. On the other hand, the private sector can bring in experience, know how, and expertise in management and operations in running the business efficiently as well as make substantial financial contribution<sup>2</sup>.

**Figure 1: Scale of Public Private Partnerships**



Source: Canadian Council for Public Private Partnerships; Deloitte

<sup>1</sup> Ernst & Young, *PPPs as Policy Instruments*, 2010.

<sup>2</sup> Asian Development Bank, *Public Private Partnership Handbook*, 2011.

PPPs are often structured in such a way that risks are allocated to the partners on the basis of ability to manage those risks. Private sector participation in project financing can take different forms, ranging from simple service or management contracts to more complex concession agreements and privatisation (Figure 1).

As the topology in figure shows, the extent of private sector participation increases as one moves from the top left of the scale (“contracting out” activities) to the bottom right of the scale (“divestiture” or full scale privatisation) where the private sector has exclusive responsibility. In a typical contracting out arrangements, such as service and management contracts, the public sector has exclusive ownership of the asset as it shoulders the entire commercial risks and cost of investment while the private sector undertakes the operation and maintenance (O & M) of the asset for a specific but renewable timeframe, say 3-5 years. In the case of a full divestiture or privatisation, however, the private sector has full control and ownership of the asset for indefinite period. In-between these two extremes lies a set of different types of relationships between public and private entities, including Concession, Build-Operate-Transfer (BOT), Build-Own-Operate (BOO) and Build-Own-Operate-Transfer (BOOT). For example, in the case of a Concession, the public sector owns the asset but the private sector is responsible for the O & M, capital investment and commercial risks for a period of 25-30 years (Table 1).

<b>Table 1: Forms of PPP and Privatisation</b>					
Option	Asset Ownership	Operation and Maintenance	Capital Investment	Commercial Risk	Duration (Years)
Service Contract	Public	Public and private	Public	Public	1–2
Management Contract	Public	Private	Public	Public	3–5
Lease	Public	Private	Public	Shared	8–15
Build-Operate-Transfer (BOT)	Private	Private	Private	Private	20–30
Concession	Public	Private	Private	Private	25–30
Privatisation	Private	Private	Private	Private	Indefinite

Source: OECD, *Private Public Partnerships for Infrastructure Financing*, Meeting of Working Groups 1 and 2 (Investment Policy and Promotion), Paris, 28-29 October 2008.

## **Motivations for PPPs**

Globally, PPPs have now become a standard mechanism for financing projects, especially large-scale infrastructure projects. As stated earlier, such an innovative financing mechanism basically recognises the relative importance of both public and private sectors in performing specific tasks and it allocates responsibilities on the basis of each partner's comparative advantages. PPPs can confer substantial benefits on both parties, and the motivations and rationales for undertaking a joint venture between the public and private entities are varied.

First, PPPs can free up government resources which can be deployed to other competing ends. Governments around the world are facing ever increasing financial constraints to develop and maintain infrastructure facilities and services due to a wide range of factors including increasing demands associated with growing populations and urbanisation, rehabilitation requirements of ageing infrastructure, and the goals of reaching previously unserved or underserved areas. These factors will continue to put tremendous pressures on infrastructure services, which will in turn put additional pressures on government finances. Globally, the global infrastructure financing gap is estimated at around US\$ 40 trillion over the next decade. In the hydrocarbon rich GCC countries, the infrastructure financing gap is estimated at US\$1.5 trillion over the next five years, suggesting that even in this wealthy region, resources may be limited to address all the infrastructure challenges. A properly structured PPP could therefore help to mobilise previously untapped resources from the private sector, thereby creating a fiscal space for the public sector, allowing the government to keep spending on other areas. The private sector will also benefit from the project through fees for services rendered and/or appropriate return on capital invested.

Second, PPPs can improve the efficiency and quality of public services through the private sector's capacity and experience in managing businesses efficiently. If the PPP is structured to allow the private sector operator to pursue its profit maximisation goal, the efficiency of infrastructure services will be enhanced considerably. Improving the efficiency of services and operations also increases the chances that those services are economically sustainable and provided at affordable rates—even after satisfying the profit requirements of the private operators. Thus, PPPs allow governments to pass operational roles to efficient private sector operators while retaining and improving focus on core public sector responsibilities, such as regulation and supervision, resulting in better and cheaper services to the consumers<sup>3</sup>.

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<sup>3</sup> Asian Development Bank, Handbook of Public Private Partnerships, 2011.

Third, PPPs can also lead to timely completion of projects. Empirical evidence from the UK and Australia clearly shows that cost and time overruns for PPP procurement are substantially lower than those for non-PPP procurement (Table 2). The transparent bidding process of PPPs can also result in efficiency gains since it helps to keep costs under control.

Improved Project Delivery	Study	Non PPP Procurement	PPP Procurement
Cost Overrun	UK	73%	22%
	Australia	35.3%	22%
Time Overrun	UK	70%	24%
	Australia	25.6%	13.2%

Source : Ernst & Young, *PPPs as Policy Instruments*, November 2010

Fourth, PPPs can mitigate project risk through a risk sharing arrangement between the public sector and the private sector. Normally, the private sector is called upon to handle operational, financial, market and completion risks. Its expertise and technical know-how can also help to reduce risk of mistakes in planning, building and operating the projects. On the other hand, the public sector is better placed to deal with political, contractual, macroeconomic, and legal risks. Risk sharing also ensures that both parties remain committed to the project on a long-term basis.

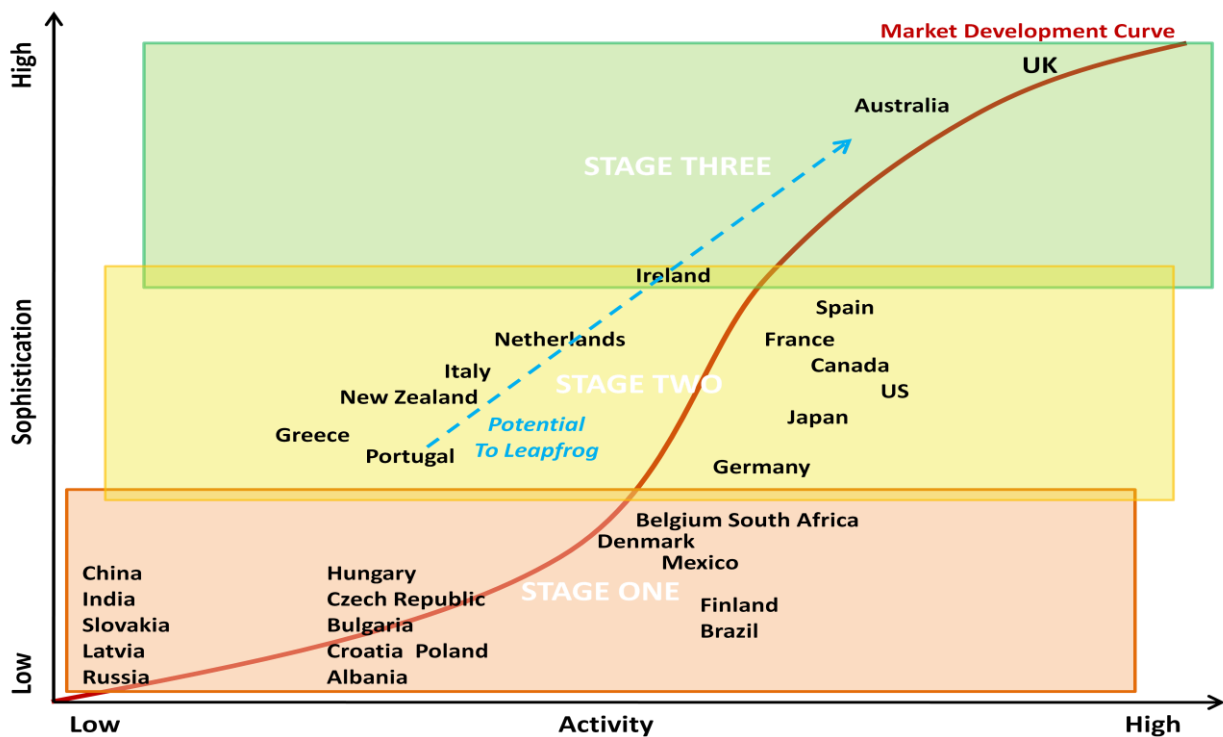
### **Global PPP Landscape**

The PPP concept is a relatively recent phenomenon, dating back to the mid-1980s. Since then, however, over 50 countries have experimented with different modes of PPPs. The UK is, however, widely acknowledged to be the country that pioneered the PPP framework through its Private Finance Initiative (PFI). Under such an initiative, the private sector designs, builds and maintains infrastructure and other capital assets and then operates those assets to sell services to the public sector. The PFI gives the private operator strong incentives to deliver the project on cost and on time, while it enables the government to spread the cost of investment over a long period of time, say 25-30 years<sup>4</sup>.

<sup>4</sup> Confederation of British Industries (CBI), *Going global: The world of public private partnerships*, 2007.

Thus, the UK, along with Australia, is considered to be at the top of PPP maturity curve, for a number of reasons including: well-defined PPP policies; well-functioning PPP units with clearly defined tasks and authorities; a well-established successful track record projects across various sectors; and a clear and ongoing access to commercial debt/project finance on attractive terms<sup>5</sup>. Other developed nations such as the US, France, Germany, New Zealand, and Canada are on the middle phase of the PPP maturity curve (Figure 2). These countries do have a successful track record of PPP projects in various sectors but their PPP policy framework is still nascent or evolving and the capacity or authority of their PPP units may need to be deepened or strengthened.

Figure 2: PPP Market Maturity Curve



Source: Going global: the world of public private partnerships, CBI 2007

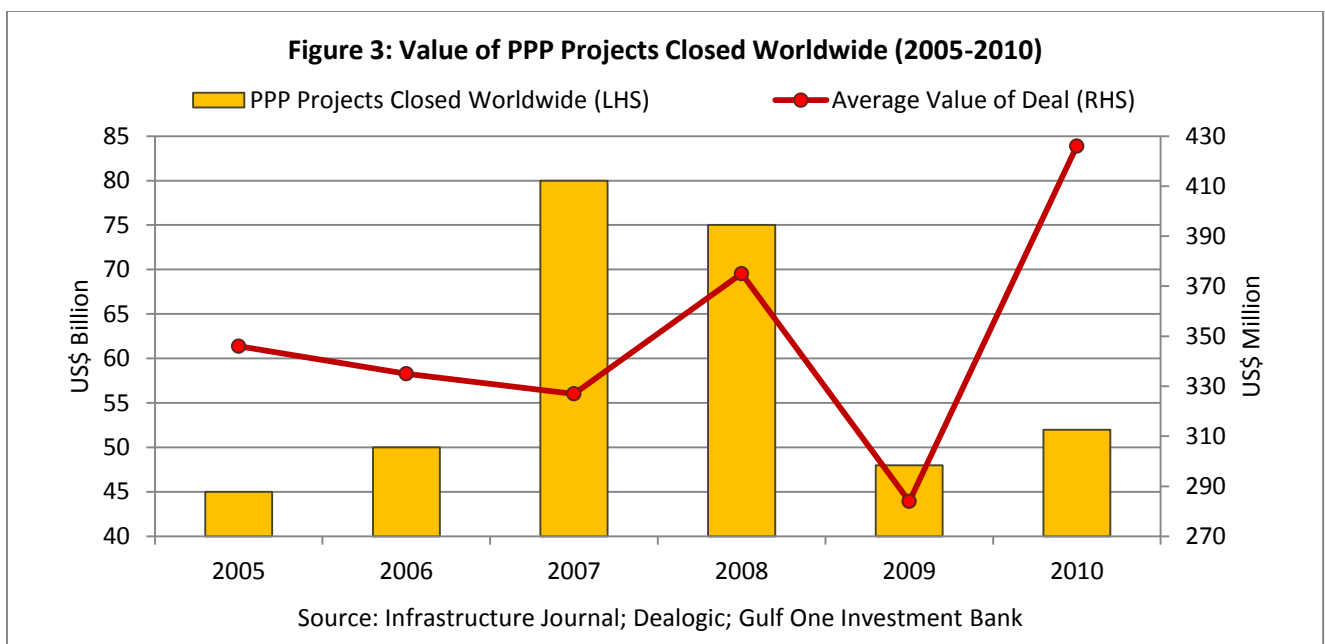
At the lower end of the PPP maturity curve are emerging economies. These countries are still lagging behind their industrialised counterparts but many of them are fast embracing the PPP concept as a standard mechanism for delivering large scale infrastructure services. Some of these countries, such as China and the

<sup>5</sup> Qatar Financial Centre Authority, *Public Private Partnerships: A Vehicle of Excellence for the Next Wave of Infrastructure Development in the GCC*, February 2012.



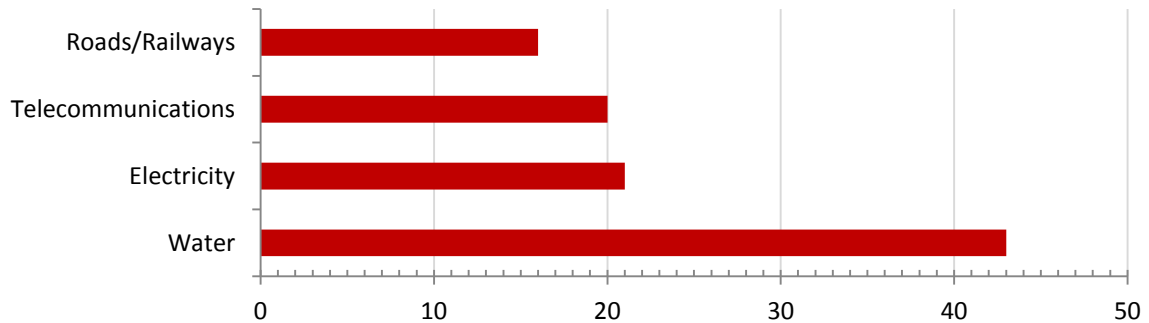
GCC countries, have delivered excellent stand-alone PPP projects or have exhibited strong success in one or two key sectors but have legal, regulatory and other policy issues to contend with.

The growing international deployment of the PPP model clearly demonstrates its attractiveness and applicability as an innovative framework for financing mega infrastructure projects. For example, over US\$1.5 trillion was spent in PPP projects around the world over the past two and half decades. And, more recently, around US\$350 billion worth of PPP projects achieved financial close with an average value of deals of around US\$448 million over the period 2005-2010 (Figure 3).



The plethora of PPP deals cut across a wide range of sectors; many physical and social infrastructure projects in the field of transport (roads, railways, airports, seaports), utilities (water and power), schools, and hospitals have been executed through the PPP mechanism. Even so, the infrastructure financing gap in these sectors is still huge with the water sector alone accounting for 43% of the projected US\$ 40 trillion of the global infrastructure investment over the next 20 years. This is followed by the electricity, telecommunications and transport sectors, with 21%, 20% and 16%, respectively (Figure 4). Undoubtedly, there will be considerable opportunity for public private partnerships in the financing of infrastructure investment in these and other sectors.

**Figure 4: Global Infrastructure Investment by Sectors (2011 – 2030)\***

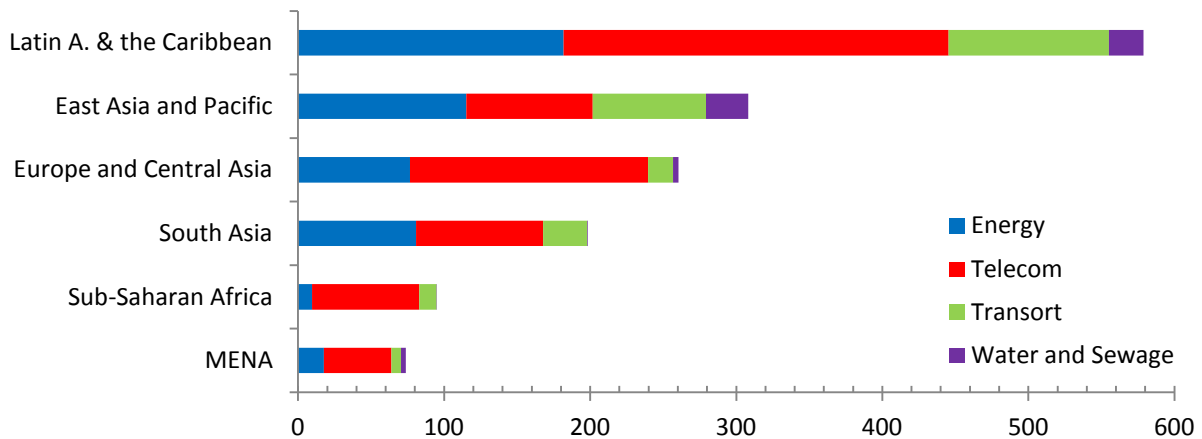


\* Total projected value = US\$41 trillion; Source: Qatar Financial Center Authority, Public Private Partnerships: A Vehicle of Excellence for the Next Wave of Infrastructure Development in the GCC, February 2012.

Although many of the success stories of PPP in infrastructure financing emanate from the developed market economies, private participation in infrastructure (PPI) in the emerging and developing economies is gaining traction, especially in the telecommunications sector. According to the World Bank data, the Latin America and the Caribbean region has dominated the developing world in terms of implementation of PPIs<sup>6</sup>, followed by East Asia and the Pacific region (Figure 5). In contrast, the Middle East and North Africa (MENA) region has had the least PPI track records.

<sup>6</sup> The World Bank PPI Project Database which records total investment in infrastructure projects with private participation, not private investment alone (<http://ppi.worldbank.org/>).

**Figure 5: PPI in Emerging & Developing Countries, 1990-2009 (US\$ Bn)**



Source: World Bank; Gulf One Investment Bank

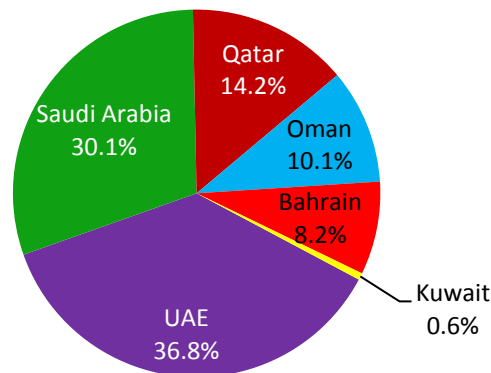
### PPPs in the GCC Region

The emergence of PPPs in the GCC region is a recent phenomenon dating back only to the beginning of this century<sup>7</sup>. The oft-cited justification for private sector involvement in infrastructure projects in the region revolves around the quest for efficiency gains in the delivery and management of such projects. This argument may, however, be overstated because despite the hydrocarbon wealth and the ongoing as well as planned mega infrastructure projects, the GCC region has a huge infrastructure financing gap of at least US\$ 1.5 trillion over the next 5 years which could not be wholly filled by the public sector. So, in addition to efficiency gains, countries in the GCC region could benefit from additional fiscal space through private sector funding.

Since 2007, there has been almost US\$ 90 billion of private project financing in the MENA countries, with the GCC region accounting for over 80% of the value of projects, according to MEED. In fact, in September 2010 alone, the value of PPP deals in the GCC region stood at US\$ 54.4 billion. The UAE and Saudi Arabia are the leading GCC countries in the region, accounting for 36% and 30%, respectively, of total PPP deals (Figure 6). Kuwait is the country in the region with the least visible presence in the PPP market but many projects have now been announced and programmed for the coming years.

<sup>7</sup> In fact, the first PPP model in the GCC region can be traced back to 1994 with the signing of Al-Manah independent power project in Oman and the subsequent signing of a project in Abu Dhabi in 1998, but the rapid adoption of the PPP framework picked up only less than a decade ago.

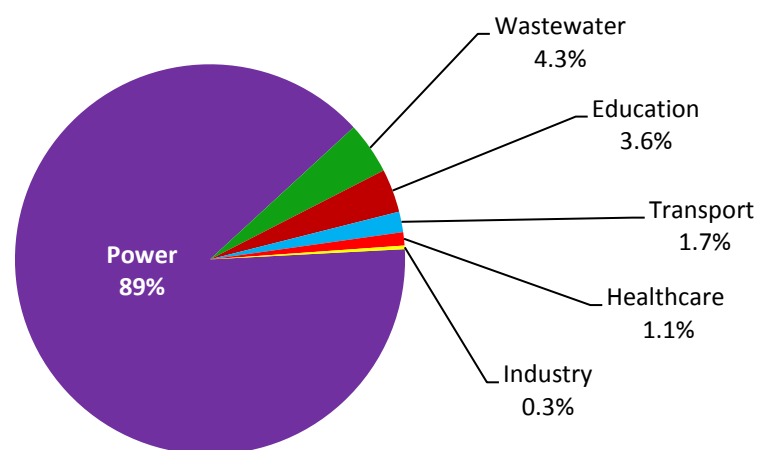
**Figure 6: Share of GCC Countries in Regional PPP Deals \***



\* Total value of GCC PPP deals as at September 2010: US\$54.4 billion  
Source: MEED, "Private partnerships win acceptance in the Middle East," February 2011.

Nearly 90% of the PPP projects in the GCC region in 2010 were in the power and water sectors executed through the Independent Water and Power Project (IWPP) initiatives. Of the remaining 10%, the wastewater and education sectors accounted for 4.3% and 3.6%, respectively, while transport (1.7%) and health (1.1%) were yet to attract significant deals (Figure7). Both sectors are, however, expected to witness a rapid increase in PPP activities in the coming years as airports and health facilities are being improved and expanded across the region.

**Figure 7: Sectoral Composition of PPP Deals in the GCC Region, Sept. 2010**



Source: MEED, "Private partnerships win acceptance in the Middle East," February 2011.

The dominance of the power and water sectors in PPP deals in the GCC region is not surprising as the first wave of public private partnerships which began in Oman and Abu Dhabi in the late 1990s were applied to

these sectors. The successful application of the PPP principle to the IWPPs in both countries led to its widespread introduction in other GCC countries.

Beside the IWPPs, success stories of PPPs in the GCC region can also be found in the education and the transport sectors. For example, around 176 schools in the cities of Abu Dhabi, Al-Ain and Al-Gharbia in the UAE are currently run by PPP operators<sup>8</sup>. In the transport sector, however, the Hajj Terminal at King Abdul Aziz Airport in Jeddah, Saudi Arabia, provides a classic example of a successful PPP deal, based on a 20-year BOT arrangement<sup>9</sup>. Outside the GCC region, Queen Alia International Airport in Jordan provides another example of a major successful PPP project in the region based on a 25-year Concession agreement.

Going forward, a number of PPP projects are being slated for execution in the GCC region, most of which are concentrated in Kuwait (Appendix Table 1). As discussed earlier, Kuwait has been playing catch-up in the PPP market, so it is now intensifying efforts to close the gap by announcing more than 30 projects to be undertaken through PPP deals in the coming years. These proposed projects transcend across sectors such as healthcare, airports, IWPP, and tourism.

Other GCC countries have proposed a wide range of mega infrastructure projects in the transport sector. Although these projects are not necessarily based on PPPs, they are likely to attract private sector participation. In the UAE, for instance, these projects include a US\$25 billion STMP-Abu Dhabi roads programme and a US\$11 billion Emirates railway project. Qatar is proposing a US\$25 billion national rail scheme while Oman and Bahrain have unveiled a US\$10 billion and US\$8.09 billion national freight and passenger railway and rapid transport network respectively. Two railway projects costing US\$6 billion each are also being undertaken in Saudi Arabia (Appendix Table 2). There is also the GCC Rail Network project which is expected to be completed by 2017. All these projects are part of a series of infrastructure development programmes in the region.

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<sup>8</sup> MEED, "Private partnerships win acceptance in the Middle East" Feb 2011, <http://www.meed.com/sectors/finance/banking/private-partnerships-win-acceptance-in-the-middle-east/3086975.article#ixzz1Pp0piM5B>

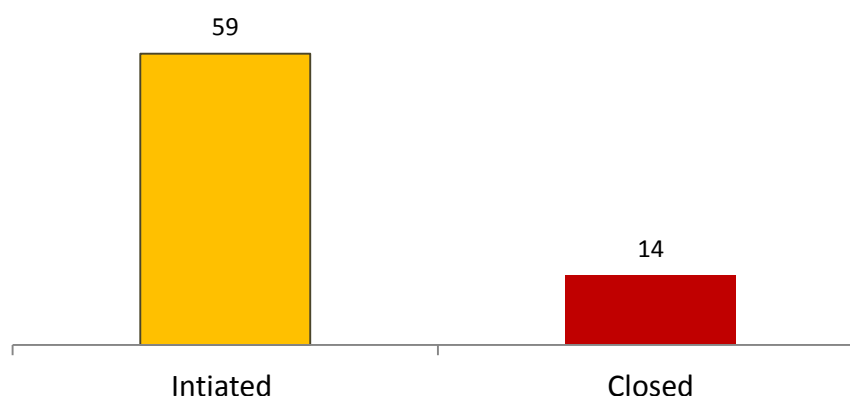
<sup>9</sup> The Hajj Terminal BOT is the first ever PPP deal that was structured based entirely on Islamic principles. Advisory services for the deal were provided by Gulf One Investment Bank.

## Challenges facing PPPs in the GCC Region

Despite a huge fanfare that greeted the introduction of PPPs in the GCC region and the success stories of the IWPP initiatives, the future of PPPs in the region still hangs in the balance due to a number of challenges. The problems were also confounded by the shelving of some of the high profile or flagship PPP projects such as the US\$ 6 billion Landbridge rail project in Saudi Arabia and the US\$ 3 billion Mafraq-Ghweifat road project in Abu Dhabi. Many other PPP deals were also either cancelled or delayed. For instance, the Tawam Hospital in Abu Dhabi, originally expected to be financed through a PPP scheme, has been cancelled.

Similarly, plans to develop car parks in Abu Dhabi through the private sector have also been shelved, just as the wastewater treatment plant at Tubli was reviewed and re-launched as an engineering, procurement and construction (EPC) project. These projects were initially perceived as a springboard for catapulting PPPs to new heights in the region, and so their cancellation and subsequent reversion back to government financing has added policy uncertainty that has consequently eroded private sector confidence. As a result, less than 25% of the PPP deals initiated in the GCC region between 2005 and 2011 actually closed (Figure 8).

**Figure 8: PPP Deals Initiated and Closed in the GCC Region (2005-2011)**



Source: Deutsche Bank, "The challenges and potential for private financing of infrastructure in the GCC", May 2011.

The scepticism of the private sector is not surprising since a cancellation of PPP deals can lead to substantial losses to investors not only in terms of financial resources and time wasted in preparing and competing for bids but also in terms of the colossal opportunity costs of these resources. According to a popular adage, "once beaten twice shy", so the recent abandonment of PPP deals in the region has sent a bad signal to investors who are unwilling to get their hands burnt again in competing for projects that might never happen.

So, what are the principal reasons for the change of heart by governments in the GCC region with regard to PPPs? There are a number of explanations but the oft-cited reason is the credit crunch that was triggered by the recent global financial crisis. The crisis severely constrained lending to the private sector and governments around the world were compelled to fill in the void through a wide range of fiscal stimuli to sustain economic activities. Governments in the GCC region spent substantial amounts of money in extra-spending in the form of fiscal stimulus, and this explains why many of the “too big to fail” PPP projects such as the Saudi Landbridge and Abu Dhabi’s Mafraq-Ghweifat projects were cancelled and are now being implemented through EPC instead of PPP.

The global financial crisis also triggered substantial capital flight out of the GCC region as foreign investors pulled their investments (both direct investment and portfolio investment) out of the region to quench the burning fires in the home countries, especially in the US and Europe. The foreign capital outflow in the UAE has been most pronounced in the region because of the significant exposure of its banks to foreign liabilities. Dubai, with a disproportionately high level of foreign investment, was subsequently hit badly by the crisis which forced the government to default on its debt repayment obligations.

The Arab uprising, which started in 2010 in Tunisia, has also put a brake on some PPP projects especially in non-GCC MENA countries. Within the GCC region, however, Bahrain is the only GCC country that experienced strong and long-lasting social unrest that nearly crippled economic activities. Oman was also affected by widespread protestations albeit for a limited period. Both Bahrain and Oman received substantial financial support from other GCC countries to enable them cope with the aftermath of the social unrest. Although other GCC countries did not experience the same level of revolt, they implemented various welfare-enhancing programmes costing around US\$ 150 billion, equivalent to 12.7% of the combined GDP of GCC countries, to assuage the concerns of their citizens. Thus, in the context of the GCC countries, the Arab uprising played little or no role in the cancellation of PPP projects but it had triggered reforms.

Clearly, the global credit crunch crisis and its aftermath provided a force majeure for the abandonment of some of the signature PPP deals, but the reality is that even prior to the 2008 financial crisis PPPs were facing serious challenges in the GCC region. One such challenge is lack of political will. This problem arises from the fact that hydrocarbon resources generate substantial revenues to the GCC governments, thereby making

them complacent and less receptive to collaborative engagement with the private sector. But PPP is most effective when government is totally committed to PPP ethos and designate a focal point or unit, usually within the finance ministry, to closely coordinate project implementation. In other words, PPPs are more effective if their execution is closely coordinated with the ministry of finance, as it facilitates synchronisation with other ministries, and thereby help to overcome bureaucratic obstacles. Being involved in the PPP will undoubtedly give the finance ministry a strong incentive to work toward the success of the project.

Experiences from around the world, especially from the OECD countries, suggest that fiscal integration is a key success factor for PPPs, but a champion within government is always needed to make PPP work because without a high-level government support for the PPP programmes, a PPP unit is most likely to be a toothless bull dog. Therefore, the success of a PPP unit crucially depends on government effectiveness, political support granted to the PPP unit, and its status within governmental structures, as lessons from a wide range of countries illustrate (Box 1).

#### **Box 1: Designing a PPP Unit – Lessons from Around the World**

A set of recent case studies conducted by Sanghi, Sundakov, and Hankinson (2011) on Bangladesh, Jamaica, the Philippines, Portugal, South Africa, United Kingdom, Korea, Australia, France, Brazil, Italy, Netherland, Poland, and Czech Republic provides the following lessons on the design of PPP units and the correlation between successful PPP programmes and the use of PPP units:

- “Less effective governments tend to have less effective PPP units. Lack of political commitment to advancing a PPP program, or lack of transparency and coordination within government agencies, will reduce the chances of success for a PPP unit. Even with a good design, a PPP unit is unlikely to be effective in such an environment. The least effective PPP units are in countries whose governments as a whole are relatively less effective.
- Without high-level political support for the PPP program, a PPP unit will most likely fail.
- Relatively successful PPP units directly target specific government failures. A clear focus on responding to particular government failures is essential in ensuring the success of the institutional solution selected.
- The authority of a PPP unit must match what it is expected to achieve. If a PPP unit is expected to provide quality control or assurance, it needs the authority to stop or alter a PPP that it perceives to be poorly designed. But this executive power must be coupled with a mandate to promote good PPPs—or the unit may simply wield a veto without adding value.



- A PPP unit's location in the government is among the most important design features, because of the importance of interagency coordination and political support for a PPP unit's objectives. In a parliamentary system of government a PPP unit is most likely to be effective if located in a strong ministry of finance or treasury. In no parliamentary systems, such as the presidential system of the Philippines and many Latin American countries, the best location for a PPP unit is less clear. In a country with a strong planning or policy coordination agency, that agency might make a natural home for a PPP unit."

Source: Apurva Sanghi, Alex Sundakov, and Denzel Hankinson, *Designing and using public private partnership units in infrastructure, lessons from case studies around the world*, June 2011.

Thus in setting up PPP units, policy makers in the GCC region should consider these fundamental points before turning to its other ingredients, such as its structure or staffing. In addition, policy makers should first think about what kinds of government failures to address and they should provide the PPP units with sufficient powers and authority to address those failures.

Within the broader MENA region, Egypt has led the way on PPP units with its May 2010 landmark PPP law. The country has established a PPP Central Unit (PPPCU), situated within the Ministry of Finance, which is responsible for the development of PPP Programmes that are based on Egypt's public sector needs and interests of the Egyptian people. The PPPCU works closely with Line Ministries and their agencies and departments to develop and implement individual PPP projects within their portfolios. The key features of Egypt's PPPCU are summarised in (Box 2). GCC countries should therefore take a cue from the Egyptian blueprint and set up the necessary structures for effective implementation of PPP projects.

#### **Box 2: Egypt's PPP Central Unit (PPPCU)**

##### **Mission Statement:**

The principal aims and objectives of the PPPCU are to:

- "Promote the national PPP initiative to key stakeholders (within Government, to private sectors, to public consumers, etc.);
- Identify and facilitate solutions to formal legal and institutional obstacles to the overall PPP project cycle;
- Develop PPP best practices, models, and standards for Egypt;
- Validate and develop PPP project proposals;
- Shepherd pilot procurements of PPPs;
- Build capacity in the public sector to identify, analyse, prepare, tender, contract, and monitor successful PPP transactions;
- Alert and stimulate private contractors and lenders to enter the new PPP market;

- Assist public infrastructure authorities in the selection of experienced and quality PPP transaction advisors;
- Work together with the public infrastructure authorities and the advisors to ensure quality and consistency in procedures;
- Ensure that set PPP principles, rules, and Standard Operating Procedures (SOPs) are followed;
- Assist awarding authorities in the transparent and competitive selection of private sector partners; and
- Report to the Ministerial PPP Committee on the progress of the PPP Project.”

**Primary Functions:**

The main functions of Egypt’s PPPCU are to:

- “Serve as the public face of PPP initiative in Egypt;
- Establish a national PPP policy framework for implementation;
- Set PPP guidelines and methodologies appropriate to Egypt;
- Assist line ministries to identify potential PPP projects as part of line ministries’ five-year strategic plans;
- Draft and issue standard project documents, contracts and PPP laws;
- Provide technical and advisory support to line ministries on project development and transaction implementation;
- Monitor project implementation post contract closure;
- Coordinate PPP Programme activities among line ministries, private sector partners and service providers, and the capital funding market;
- Identify and resolve issues that may impede successful development of Egypt’s PPP programmes;
- Act as the centre of PPP expertise, support and intelligence gatherer and disseminator; and
- Serve as a Capacity Building Centre for PPP knowledge and expertise throughout Egypt.”

Source: PPPCU Egypt, *Update on the National Program for Public Private Partnership*, June 2009.

Besides an apparent lack of PPP units and political support, the GCC region suffers from lack of adequate or sound regulatory environments for PPPs. Simplification of legal procedures as well as strengthening the institutional and administrative capacity to enforce laws, regulations and contracts will provide great incentives for PPPs in the region. It is proven that the success of PPP depends on clear and straightforward laws and regulations associated with PPP contracts and the general legal environment including procurement laws<sup>10</sup>.

<sup>10</sup> Alexander Bohmer, “Public Private Partnerships for Infrastructure Financing”, MENA-OECD Investment Programme, Private Sector Development Division.

Indeed, lack of transparent rules and regulations tends to add indirect costs to private sector seeking to forge partnership with the public sector. For example, many private sector investors tend to cite high transactions costs as one of the major challenges facing PPP deals in the region. Large tendering and contracting costs represent a real obstacle for the private sector participation as total tendering costs for some projects can reach around 3% of total project costs compared with just 1% for their conventional counterparts<sup>11</sup>. In addition, high legal fees in contract negotiations represent material indirect costs for private investors.

Yet another challenge facing the GCC countries revolves around their inability to adapt or modify imported models of PPP. Of course, countries in the region should borrow a leaf from PPP experiences around the world, but they should also strive to modify such models to reflect their own national peculiarities, local circumstances and needs. Today, countries with proven track records of PPPs have relied on PPP models which “not only take into account the government’s needs but also the social, political and demographic environments, as well as their long-term direction”<sup>12</sup>. For instance, the models used by the three most successful PPP countries (UK, Australia, and Canada) all differ from each other in several respects. As Box 3 illustrates, the UK has largely relied on the private finance initiative (PFI) model; Canada has introduced creativity to its PPP financing architecture; and Australia used two different types of PPP model to finance a number of infrastructure facilities. The GCC countries must develop institutional capability and build human capital endowments for effective adaptation and application of PPP models and approaches, as home-grown PPPs often tend to be successful.

### **Box 3: Selected PPP Models and Experiences**

#### **The UK Private Finance Initiative (PFI):**

The UK’s model of PPP is grounded in the concept of PFI, established in the 1990s. The success story of such an innovative financing framework is reflected in the large number of projects executed across a wide range of sectors over a relatively short period of time. Some of the noteworthy features of the UK PFI are as follows, according a recent report by the Qatar Financial Center Authority:

- During the past decade or so, around 10%-15% of all infrastructure projects in the UK have been financed through the PFI mechanism.
- The value of PPP projects undertaken in the UK between 2002 and 2006 ranged from \$6 billion to \$12 billion per annum, before plummeting substantially in the aftermath of the 2008 financial global crisis.
- Since then, however, the UK government has established an Infrastructure Finance Unit to provide greater financial support, which has spurred several PPP/PFI projects across a wide range of sectors,

<sup>11</sup> Ernst & Young, *PPPs as Policy Instruments*, November, 2010.

<sup>12</sup> Qatar Financial Center Authority, *Public Private Partnerships: A Vehicle of Excellence for the Next Wave of Infrastructure Development in the GCC*, February 2012.

including healthcare, education, transport and defence. In essence, the UK social infrastructure sector (healthcare and education) has been the most vibrant in terms of PPP/PFI activity, with an aggregate value of projects exceeding \$22 billion in the four years prior to the 2008 global financial crisis.

- The key drivers behind the success story of PPP in the UK revolve around: a well-defined PPP agenda; clarity about the nature of the partnership, bidding process, and contractual obligations; and predictability about the entire PPP process.

#### **Australia's PPP Models:**

Australia uses two types of PPP model simultaneously: 'core services PPP model' and 'economic privately funded project model' or 'economic model.' In the case of the core services model, mainly applied to the social sector, the government takes on the key revenue and demand risks while the private sector is responsible for ancillary services. In the case of the 'economic model', applied widely to utilities and toll roads, the private sector explicitly deals with both demand and revenue risks. Both models have been very successful in attracting long-term debt financing from banks and capital markets, with project finance consistently exceeding 80% of the project value. For example, the US\$ 3 billion Victoria Desalination project closed in September 2009 with an 83% debt component. The Australian Government has played an active role in addressing funding gaps, including accepting partially underwritten bids and providing co-lending support on a subordinated basis. All this contributes significantly to successful implementation of Australia's PPP projects.

#### **Canada's Funding Model:**

Canada differs from the UK and Australia in its approach to PPP in the sense that its PPP programme is structured on a bottom up framework, with the provinces being the main drivers of PPP activities in the country. Four of the 13 provinces in Canada (British Columbia, Ontario, Quebec and Alberta) have been at the forefront of promoting PPPs programmes. It was only in 2008 that Canada created the first federal level outfit, known as 'PPP Canada', to facilitate the development of PPP projects throughout the country. A year later, PPP Canada set up a C\$1.2 billion "PPP Canada Fund", aimed at leveraging up to C\$5 billion towards PPP projects. PPP Canada used the following criteria to assess project proposals: "(i) eligibility; (ii) public benefit; (iii) market readiness; (iv) market development; (v) PPP value for money; (vi) procurement strategy and processes; (vii) scope of private sector involvement; and (viii) revenue potential"<sup>13</sup>. Canada's PPP program is well known for efficient procurement and timely completion of projects. For example, the construction of Terminal 3 at Toronto Pearson Airport, based on a PPP arrangement, was completed ahead of schedule by 18 months.

Source: Qatar Financial Center Authority, Public Private Partnerships: A Vehicle of Excellence for the Next Wave of Infrastructure Development in the GCC, February 2012.

<sup>13</sup> Qatar Financial Center Authority, Public Private Partnerships: A Vehicle of Excellence for the Next Wave of Infrastructure Development in the GCC, February 2012.

## **Policy Options for Successful Implementation of PPPs in the GCC Region**

In spite of the recent setback on PPPs, the huge infrastructure financing gap in the GCC region has not yet vanished. As stated earlier, the region has lined up a wide range of infrastructure development programmes over the coming decades, and many of these planned projects will require massive involvement of the private sector. However, to be able to attract significant interests from the private sector, governments in the region will have to review, reassess, and address the key challenges that are militating against successful implementation of PPPs in the region.

The first step is for countries in the region to have a high-level government commitment to PPPs, preferably at Presidential (Premiership) or Vice Presidential (Deputy Premiership) level who could act as a strong champion for PPPs within government to push forward the implementation of PPP programmes. Dedicated PPP Units must be established with full powers and authorities too

Second, concrete action should be taken towards strengthening legal, regulatory and institutional framework on PPPs in the region. Some countries have started to address this issue, but much progress is still needed to allay the concerns of private sector operators. Thus a clear, transparent, and well-articulated policy framework on PPPs should be crafted and mainstreamed in national development strategies to demonstrate strong commitment to PPP implementation. A PPP-friendly environment must exist to attract investors, encourage public support, and ensure long-term project success. Addressing red tape and bureaucratic tendencies should also be given top priority as much as upgrading the region's human capital to strengthen administrative capacity.

Third, the boundary between PPPs and privatisation is often blurred and not properly clarified, sending mixed signals to stakeholders, especially among those who abhor privatisation of public infrastructure. An effective communication strategy for PPPs should be put in place to distinguish it clearly from privatisation issues. A handbook on PPP should be drafted to spell out the processes, procedures, as well as the business planning, procurement and PPP implementation issues.

Fourth, governments in the region should use sovereign wealth funds as vanguards for PPPs. SWFs should be used to facilitate the PPP process and help manage risks by providing guarantees that the private sector may request. With existing and planned public expenditures on infrastructure lagging behind 'required'

infrastructure financing, increased private and public investments in infrastructure are not only desirable but profitable considering the potentially high expected return on unlisted infrastructure asset class. Rather than stashing away funds in the West, SWFs should look inwards by investing a considerable proportion of their wealth in the region, particularly on infrastructure projects. Governments in the region should “reprioritise investments to focus on creation of competitive advantage platforms, realign SWF investment objectives to support local economies, and proactively drive the creation of regional champions and global challengers”<sup>14</sup>. Thus, the region’s SWFs should take a proactive role in leading such an ‘inward’ investment strategy by acting as catalysts for public private partnerships to finance regional infrastructure projects.

## **Conclusion**

The GCC countries have had a reasonable experience with PPPs, especially in the IWPPs using the build own operate and transfer (BOOT) framework and its variants. Outside the water and power sectors, however, progress has been very limited and tepid. A number of explanations have been advanced for the apparent lack of progress on PPP in the region, including: lack of effective PPP units and political support; weak legal and regulatory environments; weak institutional and administrative capacity; and an overwhelming reliance of the region on hydrocarbon resources which lulls governments into complacency, which in turn leads to marginalisation of the private sector and an inadequate appreciation of its role in the economic development process.

In spite of these issues, however, private sector optimism about PPPs in the region was relatively high for over a decade or so until the recent cancellations of flagship projects. Such a move has indeed dampened the appetite of private investors about PPPs in the region, and the global financial uncertainty caused by the lingering Eurozone crisis is fuelling additional scepticism. As a result, the medium-term prospects for PPPs in the GCC region look bleak despite several announcements of planned infrastructure projects. In the longer term, however, PPPs are likely to bounce back to play a critical role in infrastructure development in the region. But bringing back PPPs on track in the region is a tall order and it will take more than just the restoration of confidence in the global and regional economies. Rather, GCC countries must get out of their comfort zone and undertake the necessary reforms of the PPP environment to attract the right kinds of investments that could confer substantial benefits on their economies.

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<sup>14</sup> *Business News 24/7*, 04 February 2009.

This will require a high-level government commitment to PPPs; a clear, transparent, and well-articulated policy framework on PPPs; mainstreaming PPPs into national development strategies to demonstrate strong commitment to PPP implementation; and using SWFs as springboards for a robust promotion of PPPs in the region.

### Appendices

<b>Appendix Table 1: Selected Planned PPP Projects in the GCC Countries</b>			
	Name	Value	Remarks
Bahrain			
	The first phase of Bahrain's PPP housing plans	\$550mn	4,100 PPP housing units, of which 3,110 are social housing units. The total cost of the project will be in excess of \$550mn.
Kuwait			
	The new Umm al-Hayman waste water system	\$400mn	It will treat raw sewage that will be diverted from the Riqqa plant, which has a capacity of 180,000 cm/d and is to be decommissioned. Initial capacity of 500,000 cubic metres a day (cm/d), and associated wastewater transmission and sewage effluent networks. The second phase of construction will expand treatment capacity of 700,000 cm/d.
	The clean fuels project (CFP) and the new refinery projects (NRP)	\$30bn	
	Khiran township	\$15bn	It will have a population of more than 750,000 involving the construction of 30,000 housing units over an area of 14,500 hectares, and will be carried out in partnership with the private sector.
	Al-Zour North IWPP	KD127mn (\$455mn)	The facility will have a capacity of 1,500MW of power and 102-107 million gallons a day (g/d) of desalinated water.
	Kuwait Metro project	\$20bn	
	The hospital and related facilities, Al Andalus Area	Unkonwn	On an area of about 271,800 square metres of land and will have about 500 beds. The Health Ministry will enter into a contract for an investment term of some 25 years in addition to a design/construction term of 30 months.
Saudi			
	Expansion of King Khalid International Airport in Riyadh	SR219.5mn (\$58.5mn)	The expansion is expected to increase the airport's annual capacity to about 24 million passengers from the current 14 million. The expansion scheme will involve renovating the existing Terminal 3 and the currently unused Terminal 4, as well as adding four new concourses – A, B, C and D.

	Aircraft maintenance, repair and operation (MRO) facility at the King Abdul-Aziz International Airport Jeddah	\$800mn	Turkish firm TAV
	Hajj Terminal	\$6.7bn	Bin Laden Group
	Expansion at Medina International Airport	\$1.5bn	Turkish firm TAV
UAE			
	Hassyan IPP	\$200mn	Plans to develop an IPP at Hassyan, the first of several further IPPs and other public-private partnerships (PPPs).

Source: Various newspapers and business magazines

**Appendix Table 2: Top Ten Ongoing and Planned Projects in the GCC Region**

Country/Region	Project Value	Name	Structure	Remarks
Saudi Arabia	\$6bn	Jeddah Light Rail system		The Jeddah Light Rail system will serve a population of around 4 million people as well as easing the load on the city's infrastructure during the Hajj and Umrah pilgrimages. The light rail system will have 36 stations, with the first phase involving the building of the 25km link between the north and south of the city. The second phase will see the construction of a 14km line from east to west.
Saudi Arabia	\$6bn	Mecca–Medina Railway Link (MMRL)		The 444km railway is part of a project that will link the 2 Holy cities of Mecca and Medina through the Red Sea port of Jeddah. The project aims to ferry hundreds of thousands of pilgrims to Mecca and Medina at speeds of 360kph. Built exclusively for passenger transit, the railway will have 6 or 7 stations on its route; 3 in Jeddah, 2 in Mecca and 1 each in Medina and Rabigh near the King Abdullah Economic City.
Kuwait	\$7bn	Kuwait Metro System	PPP	A 171km long inner city transport running across Kuwait City, the Kuwait Metro System is the first metro rail project launched by the government. Only the second public private partnership project since 2009, the government will own 10% of the project and will raise 50% of the funds through an initial public offer. The remaining 40% will be held by the private developer.



Bahrain	\$8.09bn	Bahrain Rapid Transport Network		Scheduled to be completed by 2030, the project will consist of a Light Rail Transport (LRT), a monorail, trams and a Bus Rapid Transport (BRT) system that will cover 184km. The first phase of the project will include a 13km light rail track running from the Bahrain International Airport to Bahrain Mall and an 11km tramline running from Juffair to Bahrain Mall. It is expected to be completed by 2014. The second phase will consist of a 72.7km network of LRT, monorail and BRT. It is scheduled to be completed by 2021.
Kuwait	\$10bn	Kuwait National Railroad (KNRR) Network	PPP	Developed on a PPP basis, the Kuwait National Railroad Network is a project that will link the country with the Saudi borders in the south and the Iraqi borders in the north, forming part of a proposed 2,000km Gulf railway line with Iran, Iraq and beyond. The project will be developed in phases, linking up Kuwait City, Al Nawaseeb, Al Abdali, the airport and the Al Shuaiba and Bubiyan ports. The 505km long track will have the capacity of carrying 2.3 million passengers per year. In addition, the Kuwait Rapid Transit System will be 171km long and will cover the entire country.
Oman	\$10bn	National Freight and Passenger Railway		The National Freight and Passenger Railway network has been developed in response to Oman's burgeoning industrial sector. Phase I of the project will see the construction of a 280km line that will link the industrial zone of Sohar with the capital Muscat. The network will consist of a double track, a standard gauge system with a provision for high-speed trains capable of up to 350kph. Initially, however, the network will only run freight trains travelling at between 80 and 120kph. Passenger trains travelling at up to 200kph will also run on the network.
UAE	\$11bn	Emirates Railway Project		A 1,500km freight and passenger railway network stretching across the UAE, the Emirates Railway Project is an ambitious project that aims to connect the 7 emirates with Saudi Arabia and Oman. The entire project is scheduled to be completed by 2017 with the first phase of the project due to come online by 2014, linking the Shah sour gas field to Ruwais via Habshan.

GCC	\$16bn	GCC Rail Network	Initial work on the GCC wide railway project has already begun, keeping in mind its scheduled completion date at the end of 2017, according to the Secretary General of the GCC. The network will have passenger and cargo train tracks, part of a plan to boost the countries' common economies through the facilitation of trade. The network will contain one rail line of 1,970km that will connect all the GCC countries and Qatar via a bridge. A second line of 1,984km will run between Kuwait, Saudi Arabia, the UAE and Oman.
Qatar	\$25bn	Qatar National Rail Scheme	Aiming to connect the Gulf state with its GCC neighbours via the Bahrain causeway and another proposed bridge with the UAE, the Qatar National Rail Scheme will encompass a range of transport modes such as metro systems, long distance travel and freight transport. The network will also connect with Saudi Arabia via Qatar's landlink with the Kingdom. The recently formed Qatar Railways Development Company, a 51/49 joint venture between Qatar Diar and DB International, will be the sole entity responsible for developing and integrating the network.
UAE	\$25bn	STMP – Abu Dhabi Roads	Part of Abu Dhabi's 2030 Plan, the Surface Transport Master Plan is an ambitious project that includes a metro system, regional rail, a comprehensive tram network, a ferry link to Dubai and three zones of personal rapid transit. The project will also include the upgrading of the international highway and the reconstruction of the Mafraq interchange. Situated 30km away from Abu Dhabi City, the Mafraq interchange reconstruction will see traffic flow smoothed out through the introduction of main roads, bridges and flyovers. The project will see more than 330km of road upgraded, along with the creation of a number of dual carriage highways.

Source: Construction Weekly Online (<http://www.constructionweekonline.com/article-13824-top-10-infrastructure-projects-in-the-gcc/>).

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