The Investment Security in the Mediterranean Newsletter

July 2014, Issue 3

*The **Investment Security in the Mediterranean (ISMED) Support Programme** seeks to increase private infrastructure investment in the Southern Mediterranean by providing advisory services to governments on reducing the legal risk of specific projects and conducting public-private policy dialogue on broader legal framework improvements. It is implemented by the OECD Secretariat with funding by the European Commission.*

IN THIS ISSUE:

ISMED Support Programme: an Update

On 21 February 2014, the ISMED Support Programme Advisory Committee met in Paris to consider the work of the Programme since its launch in November 2012 and to chart a course to 31 December 2014. It was agreed that ISMED would develop policy recommendations to address barriers to private sector investment in MENA-region infrastructure projects with a particular focus on Public-Private Partnerships (PPPs) in the transportation and renewable energy sectors.

These recommendations will be contained in a Handbook tentatively entitled *Public-Private Partnership in the Middle East North Africa Region: A Handbook for Decisions Makers*, which will also contain best-practice guidance intended to assist government officials and policy makers in moving a project from a conceptual stage to the point where it is a viable transaction, suitable for tendering and private-sector and International Financial Institutions investment. The final version of the Handbook will be tabled during an ISMED Conference tentatively scheduled for 4 December 2014 back-to-back with the meeting of the OECD Investment Committee in Paris.

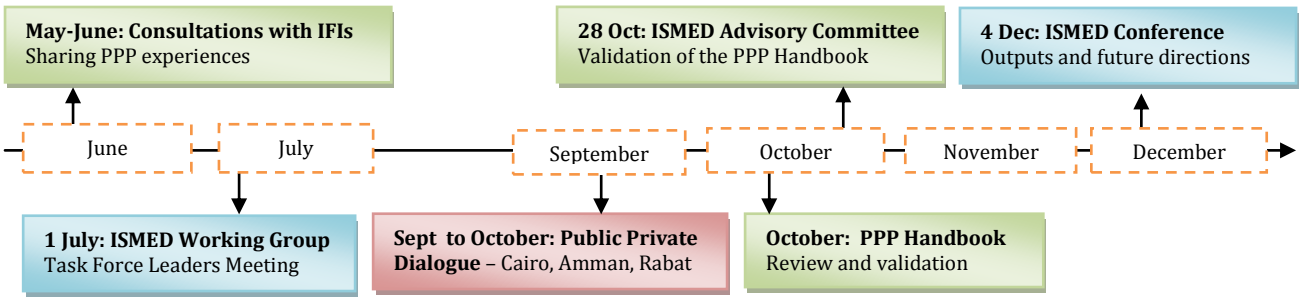
In addition to desk research, literature review, consultations with relevant institutions and OECD expertise, the ISMED Support Programme is concentrating on two work streams in formulating the content of the Handbook:
1) partnerships and consultations with International Financial Institutions (IFIs) that have experience and knowledge gained from participating in infrastructure projects in the MENA region ; and
2) findings from country-specific projects initiated during the first year of the Programme.

This newsletter provides an update on these two vital areas of our work.

A publication of the MENA-OECD Investment Programme – OECD Global Relations Secretariat. To subscribe, or cease subscription, please send an email with your contact details to mena@oecd.org. Further information about MENA-related work at the OECD can be found at *www.oecd.org/investment/psd/ismed.htm.*

With the financial assistance of the European Union

Key ISMED milestones for 2014



Consultations with international financial institutions (IFIs)

At the February ISMED Advisory Committee meeting it was agreed that member institutions would pool their deep transactional and sectorial knowledge with OECD core policy expertise via bilateral discussions and/or transmission of (case) studies relevant to the Programme. To date, consultations have taken place with the European Bank for Reconstruction and Development, the European Investment Bank, the International Finance Corporation, European Commission experts and the Multilateral Investment Guarantee Agency.

While each IFI has had different experiences and raised some unique points, some common themes have emerged from these consultations. Some of these themes are summarised below.

Government Capacity is Key

All participants agreed that government capacity is absolutely vital. Governments usually lack in-house experience with complex legal and financial transactions. It is for this reason that PPP Central Units have been developed and these should be encouraged and supported. Central units need to be staffed by individuals not only with transactional experience but who are sufficiently senior and who are trusted by the highest levels of government.

The view was widely expressed that governments in the region do not always understand the proper motivations for doing a PPP, being to harness private-sector innovation and expertise to drive value for money in the provision of public services. Instead they often turn to PPPs as a type of last resort when public finances are insufficient to fund necessary infrastructure. There is often a lack of understanding of some basic elements of PPPs and project finance. Governments can be unrealistic as to what risks can be passed off to the private sector and will usually try to transfer all risk. A lack of due diligence and study before tendering is also evident on occasion as there is a tendency to believe that the private sector will simply do what needs to be done to determine if a project is feasible. Governments sometimes seem to think of PPPs as a form of cost-free asset where the private sector does all the work, provides all financing and takes all risk.

It was also noted that some governments and government officials harbour suspicions with regard to the private sector and are uneasy with private-sector participation in the provision of public services. These views are fuelled by the sometimes corrupt practices of previous governments and by the fact that many of the economies in the region were until very recently best-characterised as command economies with the state still maintaining a high level of control. This centralised, state-centric mind-set still permeates much of the bureaucracy and political level. As high-level political support and capacity at the official level is needed to advance projects, these attitudes are not helpful.

Funding and Support Available but few Projects

There are currently very few projects in the region that feature private-sector participation and fewer still that can be considered to be PPPs. There are a number of reasons for this, chief among them being ongoing political instability in some parts of the region and investor perceptions of country risk. The small number of successful transactions results in a circular problem where governments do not have a track record and have not built capacity closing transactions and are therefore less able to attract investment and complete transactions. The importance of building a history of successfully projects as one of the most important predictors of future successful projects was emphasised. A track record is helpful for a number of reasons; it builds capacity and confidence in government on the part of investors, and lets the government know what the private sector expects.

All IFIs stated that there are more IFIs interested in projects than there are viable projects. Funding is evidently not a problem if a project is viable and developed in the right way.

Local Content Clauses and Transparency

Local content provisions in PPP tenders and contracts and transparent procurement processes were cited as important issues. Governments often try to use PPPs to build a local industry or to provide local employment. Not only can this have a negative impact on the financial aspects of the transaction and quality of labour and material inputs, it can also run afoul of IFI rules jeopardising a project's eligibility for support. It was suggested that there could be a role for the OECD in developing a methodology or guidelines on this point.

The Problem of Distortive Subsidies

There is a wide consensus that energy subsidies, prevalent throughout the region, are an issue in both transport and renewable energy. Subsidies distort the economics of transport modes making trucking for instance artificially competitive. With regard to renewable energy, electricity may not be allowed to be sold at a price that recovers cost plus profit. Therefore, the state is required to subsidise payments to the renewable producer, to enter take or pay power purchase agreements, or to provide other forms of support. From the government's point of view this support and the associated liabilities may defeat the purpose of proceeding by way of PPP.

What should be the focus of the OECD?

When asked how the OECD could best advance the prospects of PPP infrastructure projects in the region, the view was unanimously expressed that the OECD could help build government capacity to better understand and manage PPPs. A Handbook on how to best design and implement PPPs in the regional context was viewed as a very positive contribution. In addition, it was suggested, where possible, to hold capacity-building seminars using the key findings from the Handbook. The aim of the capacity building is twofold: 1) to develop, at high-levels of government, a basic understanding of PPP mechanics, including when it makes sense to proceed with a PPP and what are the building blocks of the PPP. In order to make progress, governments in the region must realize that PPPs are not a cure for a lack of public funds, that not all risk can be transferred to the private sector and that not all projects are well-suited to PPPs; 2) At the more technical level, the capacity building seminars can help strengthen the ability of government officials to advise the decision makers on when and how to make PPPs happen. The business case for PPPs must be sufficiently clear so that governments pursue the right projects, for the right reasons.

The OECD agrees with this approach and hopes to build on these suggestions. This is reflected in part by the training session planned in Egypt discussed below.

The OECD intends to conduct a number of additional consultations. At the conclusion of consultations a summary document will be drafted and circulated to all IFIs involved and other interested stakeholders.

Country Projects: an Update

Egypt

In Egypt, the Programme is working with the River Transport Authority (RTA) to assist in developing a river ports project on the Nile. A Draft Final Report has been delivered reviewing lessons learned from a previous attempt to develop river ports in 2009-10 and providing suggestions and guidance on the way forward. It is expected that the report will be finalised by the end of July. A workshop gathering public and private stakeholders to discuss the Final Report and the River Ports Project will be held in Cairo in September.

In addition, the Programme will be providing a training session in PPP fundamentals to the RTA in September. The training session, to be conducted in co-operation with international financial institutions, is expected to be the first of a number to be held with MENA governments to build on and implement the recommendations of the Handbook.

Morocco

In Morocco, the programme has undertaking a benchmarking study of legal frameworks for logistics zones development as requested by the Agence Marocaine de Développement de la Logistique (AMDL).

A mission was undertaken from 16-20 June to meet public and private stakeholders and gather information for the study which is expected to be final by October. A public-private workshop is planned for October in Rabat to discuss the findings of the study.

Jordan

In Jordan, the Programme is working on a study of an optimal incentives framework for renewable energy infrastructure on behalf of the Ministry of Environment. Renewables will form a vital component of the Kingdom's future energy supply and the government is currently defining strategic orientations and policies.

A week-long mission to Amman was conducted starting 23 June to gather information and meet the important players in the Jordanian renewable energy industry. A public-private dialogue workshop will be held in September prior to finalisation of the study in October.

Refining the PPP Handbook

The Handbook is one of the major work outputs of the ISMED Support Programme. It will reflect the work and experiences of the Programme and the insight gained from co-operation and consultation with IFIs. For this reason, and to further refine the Handbook, the Programme will provide an early draft by end of August to all IFIs that have participated in consultations.

The Handbook will be further validated at the 28 October meeting of the ISMED Advisory Committee. The final Handbook will be presented at the ISMED Conference scheduled for 4 December in Paris.

Legal Investment Protection Study

The Study on *Protecting Investment in Arab Countries in Transition: Legal Frameworks for Infrastructure Investment in Egypt, Jordan, Morocco and Tunisia* was presented to the OECD Investment Committee in Paris on 25 June. The report prepared by the Investment Division looks at protection provisions contained in domestic legal frameworks and investment treaties of each of the four countries, sheds light on legal gaps and suggests policy options for strengthening further the legal environment for investment, in particular infrastructure.

The report and its recommendations were well received by delegates who were invited to provide comments. It will be further discussed with beneficiary's countries and presented at the December 2014 ISMED Conference. Delegates welcomed the recommendations of the report and its integration to other outputs of the ISMED Support Programme, the MENA-OECD Investment Programme and the Investment Division.

The ISMED Working Group

The ISMED Working Group Inaugural Conference (9 December 2013): opening remarks by Ms Elisabeth Guigou, French MP.

Launched on 9 December 2013 at an Inaugural Conference held in Paris, *"Fostering Infrastructure Investment and Mitigating Risk in Uncertain Times"*, in the presence of Mr Rintaro Tamaki, Deputy Secretary-General (OECD), H.E. Mr Mohamed Louafa, Minister Delegate to the Head of Government, in charge of General Affairs and Governance (Morocco) and Ms Elisabeth Guigou, Chair of the Foreign Affairs Committee of the French National Assembly (France), the ISMED Working Group is designed as a forum where OECD and MENA governments, representatives of international financial institutions, development agencies, private-sector operators, lenders and investors, can share expertise, formulate recommendations and lend support to regional and domestic policy measures.

In 2014, the Working Group will seek to address means and ways to facilitate private sector investment in infrastructure projects throughout the MENA region, under public-private partnership (PPP) structures, through arbitration and the use of guarantee instruments.

Participants stressed the importance of infrastructure investment for economic growth and development, and called for innovative approaches to infrastructure financing and enhancing the efficiency of legal investment protection measures and risk mitigation instruments.

Under the co-chairmanship of France and Iraq, it was agreed that research-based recommendations would be submitted to the next meeting of the Working Group in December 2014 in four subject areas:

- Project finance and cost-sharing;
- Commercial arbitration;
- Public-private partnerships and risk sharing;
- Islamic finance instruments.

From left to right: Rintaro Tamaki (OECD), Pascale Andreani (France), Mohamed Louafa (Morocco), Fareed Yasseen (Iraq), Marcos Bonturi and Alexander Böhmer (OECD).

Four task forces have been formed along these lines, gathering experts from diverse backgrounds, to developing the recommendations.

The task forces have met regularly since the December launch event and the Leaders of the respective task forces submitted their draft recommendations during a coordination meeting on 1 July in Paris.

Relevant OECD instruments

The Policy Framework for Investment

The PFI is a tool providing a checklist of issues for consideration by any government interested in creating an attractive investment environment and in enhancing the development benefits of investment to society. The policy areas covered are widely recognised, including in the Monterrey Consensus, as underpinning a healthy environment for all investors, from small-and medium-sized firms to multinational enterprises. The PFI is currently under revision.

OECD Principles for Private Sector Participation in Infrastructure

These OECD Principles aim to help governments work with private sector partners to finance and bring to fruition infrastructure projects in areas of vital economic importance such as transport, water and power supply and telecommunications. They offer governments a checklist of policy issues to consider in ensuring that citizens get the services they need at a fair cost and with viable returns to private sector partners.

OECD Principles for Public Governance of Public-Private Partnerships

These OECD Principles provide concrete guidance to policy makers on how to make sure that Public-Private Partnerships (PPP) represent value for money for the public sector. In concrete terms, the Principles will help ensure that new projects add value and will stop bad projects going forward. They provide guidance on when a PPP is relevant – *e.g*. not for projects with rapidly changing technology such as IT, but possibly for well known generic technology such as roads. They focus on how to get public sector areas aligned for this to work: institutional design, regulation, competition, budgetary transparency, fiscal policy and integrity at all levels of government.

Find these instruments online at: www.oecd.org/daf/investment/instruments

Contacts

Mr Andrew Fitzpatrick
Acting Coordinator
ISMED Support Programme
Andrew.Fitzpatrick@oecd.org

Ms Véronique Zovaro
Policy Analyst
ISMED Support Programme
Véronique.Zovaro@oecd.org

Mr Sabri Draia
Junior Policy Analyst
ISMED Support Programme
Sabri.Draia@oecd.org

www.oecd.org/mena/investment