

Public Private Partnerships—infrastructure

- 7.1 In announcing Australia’s new development policy, the Minister for Foreign Affairs highlighted the importance of ‘tackling infrastructure bottlenecks in our region which are hampering economic growth’, and reaffirmed the importance of private sector support.¹
- 7.2 The private sector is a major beneficiary of infrastructure investment. It can make a sizeable contribution to the provision and maintenance of infrastructure, particularly through complex large scale projects, which may involve Public Private Partnerships (PPPs).

Infrastructure needs in developing countries

- 7.3 In addition to energy, communications, transport infrastructure and water, there is a need for social infrastructure such as hospitals, education facilities and public housing.²
- 7.4 Financing infrastructure investment was identified as a priority by the G20 under Australia’s presidency in 2014.³ The Asian Development Bank (ADB) stated ‘the Asia and Pacific region requires infrastructure investment of at least \$8 trillion until 2020’.⁴ Inadequate infrastructure has a huge impact at the country level.

1 The Hon Julie Bishop MP, Minister for Foreign Affairs, ‘The new aid paradigm’, *Speech*, delivered 18 June 2014.

2 Department of Foreign Affairs and Trade, (DFAT), *Submission 21*, p. 24.

3 Mr Sam Gerovich, First Assistant Secretary, DFAT, *Committee Hansard*, Canberra, 23 June 2014, p. 2.

4 Asian Development Bank (ADB), *Submission 120*, p. 2

7.5 The ADB also suggested that Australia is well placed to support investments in infrastructure in the Indo-Pacific Region:

Australia is home to many of the world's leading infrastructure investment managers – by some counts, the Macquarie Group is the world's largest and most prominent infrastructure investment manager. Macquarie has won mandates to manage infrastructure funds in a number of developing member countries and most recently it secured the management mandate of the Philippine Investment Alliance for Infrastructure, a US\$685 million private equity fund, formed with local and international pension funds and ADB. The fund prioritizes investments in PPPs and other infrastructure sector investments.⁵

7.6 The ANZ also suggested:

Australian companies are highly skilled in different aspects of infrastructure provision, including for electricity, ports, telecommunications and water. ANZ finances essential infrastructure projects by state-owned enterprises and provides high-level expertise in many developing markets. Australia is also a leading supplier of natural resources and energy, food and agriculture, and health and education services.⁶

7.7 There are particular needs in the Pacific:

- The World Bank Group observed that only 20 per cent of households have access to electricity, short runways limit the types of aircraft that can land, and internet costs are amongst the highest in the world.⁷
- Holland Commodities International contended that the lack of infrastructure such as wharves and storage facilities limit access for ships to collect cargo, which ultimately reduces export capacity and potential for economic growth.⁸

7.8 For businesses, lack of infrastructure limits economic opportunities. For smaller enterprises, including in agriculture, the Australian Centre for International Agricultural Research (ACIAR) advised:

Several elements underpinning agricultural growth need to be considered...physical infrastructure including irrigation, roads, storage, power supply and telecommunications networks – especially the 'last mile' to reach all farmers.⁹

5 ADB, *Submission 120*, p 3.

6 ANZ, *Submission 48*, p. 6.

7 World Bank Group, *Submission 75*, p. 10.

8 Holland Commodities International Pty Ltd, *Submission 4*, p. 2.

9 Australian Centre for International Agricultural Research (ACIAR), *Submission 22*, p. 7.

7.9 Lack of infrastructure also has a significant impact on the livelihoods of individuals, and especially women. The International Women’s Development Agency observed:

Improvements to rural water and irrigation systems and transportation infrastructure reduce the amount of time women spend on arduous tasks such as fetching water and tending family crops. These investments will bring returns in the form of increased women’s engagement in market-based activities, greater productivity and reduced time burden.¹⁰

7.10 Governments in the Indo-Pacific region find it challenging to provide the infrastructure needed. Adam Smith International submitted:

Countries in the Indo-Pacific often struggle to deliver public projects on time and to cost. Poor governance is the root cause of many of the challenges. Combinations of inadequate planning, poor project implementation and perceptions of corruption among officials diminish the return on capital spend and normally result in a misallocation of public resources. The result is that developing countries typically achieve very poor value for money in infrastructure, and achieve little development impact.¹¹

7.11 The ADB Private Sector Development Initiative also observed that where public infrastructure has been provided, a lack of maintenance has resulted in rapid deterioration.¹² ADB further noted that, in the Pacific, state owned enterprises ‘absorb large amounts of scarce capital, on which they provide very low returns’:

Many commercial SOEs compete with the private sector, yet do so with the benefit of subsidized debt and equity. Meanwhile, the infrastructure SOEs – usually monopoly providers of goods and services such as power, ports, water and airports – are often inefficient, driving up input costs for the private sector and draining government budget resources that could be better spent elsewhere.¹³

7.12 Noting the significant infrastructure needs in developing countries, Adam Smith International suggested that ‘[m]ost governments have inadequate resources and public savings to finance the infrastructure they require.’¹⁴

10 International Women’s Development Agency Inc. *Submission 122*, pp. 13-14.

11 Adam Smith International, *Submission 17*, p. 3.

12 ADB PSDI, *Submission 87*, p. 10.

13 ADB PSDI, *Submission 87*, pp. 9-10.

14 Adam Smith International, *Submission 17*, p. 3.

7.13 The ADB stated that bilateral and multilateral development finance ‘can meet only a small part of the region’s needs for investment in economic and social infrastructure and public services.’¹⁵ In order to fund the provision of additional infrastructure, the ADB suggested countries have three options:

- review traditional sources of funds and explore additional funding from them;
- investigate mechanisms for generating more financial resources from off-budget sources; and
- consider a greater role for PPPs in procuring infrastructure and identifying and addressing impediments to the development of PPP transactions.¹⁶

Sovereign Wealth Funds

7.14 Oil Search observed that by setting up and effectively managing a Sovereign Wealth Fund (SWF), governments such as that of Papua New Guinea (PNG) can address infrastructure needs.¹⁷ Further, Pacific Islands Trade and Invest suggested that:

...DFAT considers working in partnership with Australian financial institutions to establish and manage sovereign wealth funds (SWF) in countries where no such investment funds exist. We see a great opportunity to extend this service to help countries meet the longer-term maintenance and operating costs of social and economic infrastructure and services.¹⁸

7.15 The Australian Government has been supporting the establishment of SWFs through both bilateral initiatives, including assisting PNG with technical advice and capacity building, and as a founding member of the International Forum of Sovereign Wealth Funds (IFSWF).¹⁹

7.16 The IFSWF is a voluntary group of SWFs. In addition to providing a forum for the exchange of views amongst SWFs, the IFSWF developed the ‘Santiago Principles’, ‘which are a voluntary set of principles and practices identifying appropriate governance and accountability arrangements for SWFs, as well as prudent and sound SWF investment practices’.²⁰

15 ADB, *Submission 120*, p. 2.

16 ADB, *Submission 120*, p. 2.

17 Mr Peter Botten CBE, Managing Director, Oil Search Ltd, *Committee Hansard*, Canberra, 29 August 2014, p. 3.

18 Pacific Islands Trade and Invest, *Submission 60*, p. 2

19 Department of Finance, ‘International engagement’, <www.finance.gov.au/investment-funds/international-engagement.htm>, viewed 19 May 2015.

20 Department of Finance, ‘International engagement’, <www.finance.gov.au/investment-funds/international-engagement.htm>, viewed 19 May 2015.

- 7.17 Noting that SWFs go to the heart of sovereignty and long-term independence of a nation, the Committee found that the Australian Government's current activities, providing capacity support and continued involvement in the IFSWF, are an appropriate way to promote SWFs with development partners. In addition, the Committee endorses the suggestion made by Pacific Islands Trade and Invest in relation to DFAT examining options, possibly through the innovationXchange, to engage Australia's financial institutions to provide services related to the establishment and management of SWFs.

Recommendation 16

The Committee recommends that the Department of Foreign Affairs and Trade leverage the expertise of other Australian Government agencies, including the Department of Finance and the Future Fund, as well as Australia's financial institutions in order to further promote the establishment and management of sovereign wealth funds for development partners.

The role of the private sector in government financed infrastructure

- 7.18 Transparency International stated:
- Around the world, municipal and national governments use public procurement processes to build roads, provide school textbooks, stock medical clinics and construct drinking water systems. These different activities account for a public contracting market that is estimated globally at US\$ 2 trillion.²¹
- 7.19 The Overseas Development Institute also observed that donor funded infrastructure projects 'rely heavily on direct contracting of construction companies to carry out this work.'²² This may exclude the engagement of local contractors.
- 7.20 Governments may also indirectly fund infrastructure delivered by private companies. For instance, under the tax credit scheme which operates in Papua New Guinea, resource companies provide infrastructure and offset

21 Transparency International, *Submission 41*, p. 2.

22 Overseas Development Institute, *Submission 51*, p. 5.

the costs of doing so against tax payments. The past president of the Australia Papua New Guinea Business Council observed:

... we believe that better outcomes by as much as 50 per cent can be achieved for the same amount of money by not channelling the money through a government agency because, among other things, there is leakage and overpayment for the same result. I suppose, at the end of the day, the biggest concern is the quality of the product... it is in the interests of whoever the developer is, reputation-wise, to make sure they deliver a good product, so they do that.²³

7.21 Oil Search, whose annual budget for infrastructure exceeds \$100 million, described how it works with governments to provide infrastructure:

...Oil Search provides project management and construction skills to deliver these projects, using government money in the form of tax credits, in an efficient and transparent way. Oil Search is also providing capacity building within Government Departments that administer these projects, thereby providing a growing platform for the Government to increase their efficiency in delivery of this core infrastructure.

The roads, schools and hospitals provide the backbone for further economic growth in previously remote areas around the country. These partnerships are beneficial to the Government, the people in the impacted areas and the Company in building its relationships and reputation, whilst providing a stable operating environment for its operations.²⁴

7.22 Government and donor contracts are not confined to large scale infrastructure. Cardno described how, under a \$27 million Australian government contract, it is supporting the Timor-Leste Government implement a \$250 million community infrastructure program:

We have trained up engineers and social facilitators to go out to every single village in Timor-Leste to identify what their community infrastructure development needs are, whether that be a toilet block, a community hall, an addition to a school building, a road or a bridge or something like that... They receive a rolling

23 Mr Peter Taylor, Past President, Australia Papua New Guinea Business Council, *Committee Hansard*, Sydney, 7 November 2014, p. 20.

24 Oil Search Limited, *Submission 104*, pp. 1-2.

grant every year of another \$50,000, provided they build and maintain that infrastructure and it achieves its intended purpose.²⁵

7.23 Supporting governments to manage procurement processes and contracts was highlighted in the evidence. DFAT stated it is:

Promoting increased and more effective use of private sector contractors by public sector agencies, for example piloting performance-based approaches for road maintenance by contract and for water connections.²⁶

7.24 Noting the potential for bribery in the public works and construction sector, Transparency International referred to the importance of transparent procurement and high public financial management standards and noted:

Efforts being led by the Construction Sector Transparency Initiative (CoST), the Global Initiative on Fiscal Transparency (GIFT), the Open Contracting Initiative and the Open Government Partnership (OGP) represent important multilateral processes that are setting a new and common bar for what is transparent and accountable procurement, including the full range of documents that should be publicly disclosed.²⁷

7.25 The Committee's evidence clearly demonstrated that the infrastructure needs in developing countries are significant, and that current government and donor budgets are not sufficient to meet the needs. Roads, hospitals, power supply, sanitation and other infrastructure are required to support greater economic growth and poverty reduction.

7.26 To address these needs governments are increasingly looking to attract finance from the private sector. However, with the large sums of money involved, transparency and strong governance mechanisms must be in place.

7.27 Australia is providing some excellent examples of enterprises which are using tax credits to help build infrastructure.

25 Mr Mark Pruden, International Development Business Unit Manager (Asia Pacific), Cardno Pty Ltd, *Committee Hansard*, Melbourne, 15 August 2014, p. 23.

26 DFAT, *Submission 21*, p. 39.

27 Transparency International, *Submission 41*, p. 3.

Recommendation 17

The Committee recommends that the Australian Government:

- participate in or support joint ventures between the private and public sectors, and wherever possible ensure technology transfer and local contractors are engaged; and
- as a means to mobilising domestic financial resources, provide capacity building assistance to partner governments to develop effective and transparent governance frameworks to support tax credits being used for building infrastructure.

Public Private Partnerships

7.28 Australia, often through multi-donor platforms managed by multilateral development banks, is supporting countries to develop PPPs and attract private financing for these projects. This support includes helping to develop legal and regulatory frameworks and building the capacity of governments to manage PPPs.

7.29 PPPs are contractual arrangements between the private sector and national (or subnational) governments.²⁸ The Overseas Development Institute noted that PPPs 'should be viewed as mutually beneficial business partnerships rather than mechanisms for aid delivery.'²⁹

7.30 In discussing the benefits of PPPs in health, Abt JTA noted that PPPs can support government policy goals by:

- Making capital expenditures affordable in the near term;
- Providing Government budget stability through defined and predictable health expenditures;
- Transferring risk to the private sector for construction delays or cost overruns for a large and complex building project;
- Transferring significant operational risk for the delivery of complex health care services, while capturing the efficiencies of private sector management; and
- Providing an economic engine for growth for locally owned businesses.³⁰

28 Development Policy Centre, *Submission 103*, p. 4; DFAT, *Submission 21*, p. 24.

29 Overseas Development Institute, *Submission 51*, p. 6.

30 Abt JTA, *Submission 5*, p. 3.

7.31 ADB observed that PPPs are not a panacea, and the ‘most successful PPPs are not just about finance, but rather those successes have had a focus on long-term delivery of services and a “fit for purpose” infrastructure services solutions.’³¹ ADB further suggested:

PPP should be chosen when it represents better ‘value-for-money’ compared to traditional infrastructure procurement. Better value-for-money can be accomplished when the PPP procurement delivers high-quality services at a lower cost than traditional infrastructure procurement, and the private sector is more experienced to manage such services than the public sector.³²

7.32 The World Bank Group considers that a ‘well-structured PPP can deliver greater efficiency in the use of resources, stronger performance incentives, improved governance and greater transparency’.³³ On the latter point, it noted:

...by using a PPP process, a government will typically face enhanced scrutiny by outside parties, such as lenders and investors, whose capital will be at risk over the long-term, and dependent on the performance of service delivery. The increased scrutiny of the long-term commitment required under a PPP usually requires information about the true long-term risks – and therefore costs – to deliver the public service. This scrutiny can generate a more informed and realistic debate on project selection, and a focus on outputs and outcomes.³⁴

7.33 The Overseas Development Institute highlighted the importance of well-designed contractual arrangements for PPPs:

One of the key determinants of the success of private-public partnerships to develop infrastructure is in making sure that the contractual agreement between parties is clear, transparent, enforceable and has accurately assessed the risks associated with the investment and how these risks will be shared by the parties. ...Successful public private partnerships require a clear legal and regulatory framework to be in place which supports the drafting and implementation of these agreements; competent and accountable public authorities to manage the state commitment to such contracts; the presence of a selection of private sector

31 ADB, *Submission 120*, pp. 2-3.

32 ADB, *Submission 120*, pp. 2-3.

33 World Bank Group, *Submission 75*, p. 3.

34 World Bank Group, *Submission 75*, p. 3.

companies with sufficient technical and financial capacity to participate in such investments.³⁵

7.34 Despite the benefits of a well-designed and implemented PPP, Oxfam Australia raised concerns about PPPs, suggesting that for some projects there had been a lack of:

- accountability for social, health, livelihood, food security, and gender impacts, in the absence of adequate monitoring and evaluation of projects or grievance mechanisms for affected communities;
- transparency, for example, on benefit sharing, social and environmental impacts, and food security implications;
- participation by governments, workers and communities in project design and implementation, including free, prior, and informed consent of affected communities and their members;
- demonstrable focus on rights, sustainability, and empowerment;
- attention to benefiting women and including them in decision making;
- alignment with national government policy or international guidelines, for example, the Voluntary Guidelines on the Responsible Governance of Tenure of Land, Fisheries and Forests in the Context of National Food Security, or national government policy.³⁶

7.35 Both Oxfam Australia and the Australian Council for International Development (ACFID) encouraged careful assessment and consultation prior to implementation. ACFID observed that impacts of large scale infrastructure, including those delivered through PPPs, should be 'properly identified, accounted for and mitigated in line with the specific social and environmental risks they may pose, either definitely or potentially'. ACFID further cautioned:

Often large-scale infrastructure can have flow-on effects such as involuntary displacement of local people, abrogation of indigenous custom, and/or destroying physical cultural resources. These can be coupled with environmental impacts such as degradation of land, air or water quality; and/or other natural resource depletion.³⁷

35 Overseas Development Institute, *Submission 51*, p. 6.

36 Oxfam Australia, *Submission 72*, pp. 23-24.

37 Oxfam Australia, *Submission 72*, p. 24; Australian Council for International Development (ACFID), *Submission 52*, pp. 19-20.

7.36 The then B20 Sherpa, Mr Milliner, observed that consultation and coordination efforts are improving, and in the context of the cross border planning of infrastructure in Africa:

There are a whole series of people [from] a mixture of public and private industries and NGOs who are all working with African governments around the planning and prioritisation of a whole series of basically nation-state building infrastructure assets through Africa. I think that is a good example of where they are trying to coordinate at the right level. Ultimately then it will have to be implemented at a state level where it will involve procurement processes and all those things.³⁸

Government capacity building and safeguards

7.37 Highlighting the complexity of PPP arrangements, DFAT stated:

[PPPs] have worked to draw in private investment for public assets and services, but the contractual arrangements are complex and special skills are needed to negotiate and manage them effectively. These skills are particularly difficult for developing country governments with low capacity to access and retain.³⁹

7.38 The Committee found that the Australian Government and the international private sector can help to address these capacity constraints. As noted by Jacobs, 'one of the challenges then is how we ensure that recipient governments have capacity to manage and ensure we get the right outcomes'.⁴⁰ Jacobs suggested governments are 'looking to places like us to see how they can do more and how they can learn. That is also the opportunity, in leading organisational capacity strengthening for these groups.'⁴¹

7.39 Mr Milliner noted that the B20 was working with multilateral development agencies to provide recommendations on infrastructure to the G20, and that:

What we need to do is to increase substantially the capability in those countries. Quite often it is done on a one-off project basis where the [multilateral development banks] will come in and provide the capacity-building piece around a particular project, either at a government, administrative or bureaucratic level

38 Mr Robert Milliner, B20 Sherpa, B20 Australia, *Committee Hansard*, Canberra, 18 June 2014, p. 4.

39 DFAT, *Submission 21*, p. 24.

40 Dr Michael Shirley, Group Vice President, Infrastructure and Environment, Jacobs, *Committee Hansard*, Melbourne, 15 August 2014, p. 34.

41 Dr Michael Shirley, Jacobs, *Committee Hansard*, Melbourne, 15 August 2014, p. 36.

around the procurement process, funding and funding arrangements – getting through laws and everything in place... We work through with the various agencies how that expertise is used in a more sustainable way so that we can actually accelerate the rate of investment.⁴²

7.40 Complex Program Group noted that institutional development is ‘generally a long-term and progressive process’ and suggested:

- using simple management contracts and leases, which can be managed by the native government, as a first step towards establishing a private sector presence; or
- using sophisticated PPPs (namely, the Inverted Bid Model) that establish their own internal governance and contract management system, and that can be contract managed by an external entity with appropriate expertise;
- that an independent expert team should initially manage the project using best-practice project and contract management processes (and as part of the project’s required outcomes, progressively mentor and coach local government teams, as well as contextualise the best-practice processes).⁴³

7.41 Complex Program Group further observed that PPPs can be used to build the capacity of firms in developing countries by requiring organisations with responsibility for the overall project to engage firms on terms that are:

... specifically tailored to foster local capability development, as well as address other key Sustainability Development Goals (SDGs) such as the increased participation of women and minorities in the workforce.⁴⁴

7.42 Adam Smith International expressed concern that under DFAT’s Adviser Remuneration Framework ‘DFAT is pricing itself out of the market for quality companies and quality advisers’, and suggested:

DFAT should give itself the space in the foreign aid program to appoint high-quality Australian professional services companies and management consultancy companies that do fantastic work around things like PPPs with the state level governments in Australia that at the moment do not work on the foreign aid program.⁴⁵

42 Mr Robert Milliner, B20 Sherpa, B20 Australia, *Committee Hansard*, Canberra, 18 June 2014, p. 2.

43 Complex Program Group, *Submission 154*, p. 2.

44 Complex Program Group, *Submission 154*, p. 5.

45 Mr Jonathan Pell, Director, Asia Pacific, Adam Smith International, *Committee Hansard*, Sydney 20 August 2014, p. 58.

7.43 Oxfam Australia further recommended that when funding PPPs the Australia Government ensure:

- assessments on the suitability (including long term costs) of the model are done;
- appropriate levels of stakeholder consultation;
- there are safeguard procedures and redress mechanisms; and
- the partner Government has appropriate legal and regulatory mechanisms to deliver a PPP.⁴⁶

7.44 Similar recommendations were made by ACFID, which encouraged the Australian Government to ensure that any PPPs funded by Australia comply with World Bank social, legal and environmental safeguards⁴⁷ and that:

The Australian Government should follow the lead of the Asian Development Bank and appoint Principle Sector Specialists on Safeguards. The role would be responsible for ensuring coordination of, compliance with, and capacity development on, adherence to safeguards for development both in Canberra and at Post.⁴⁸

7.45 DFAT is preparing an infrastructure strategy, and has outlined its current approach:

[It] does not solely focus on physical infrastructure. It also focuses on the governance and policy arrangements needed to provide safe, sustainable and reliable infrastructure. Partner delivery systems need to be carefully evaluated and sometimes strengthened; civil society engaged; feasibility studies and detailed engineering designs prepared; and open and transparent procurement processes carried out, before works can begin. As a result infrastructure programs have long lead times.⁴⁹

7.46 DFAT acknowledges the need for safeguards:

The effective development of infrastructure requires appropriate action to safeguard communities and infrastructure investments from environmental and displacement/resettlement risks. It is

46 Oxfam Australia, *Submission 72*, pp. 25-26.

47 For further information on the safeguards, see World Bank, 'Safeguard policies', <web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/EXTPOLICIES/EXTSAFEPOL/0,,menuPK:584441~pagePK:64168427~piPK:64168435~theSitePK:584435,00.html>.

48 ACFID, *Submission 52*, p. 19.

49 DFAT, Infrastructure, <www.dfat.gov.au/aid/topics/investment-priorities/infrastructure-trade-facilitation-international-competitiveness/infrastructure/Pages/infrastructure.aspx> viewed 1 April 2015.

important that gender and access for people with disabilities are also integrated into infrastructure activities to support inclusive development.⁵⁰

- 7.47 PPPs can complement other models of public and private infrastructure provision. However, the Committee also notes the complexity of providing large scale infrastructure, particularly through PPP arrangements. Appropriate safeguards must be in place to address social and environmental issues, including potentially the resettlement of communities.

Recommendation 18

The Committee recommends that the Australian Government follow the World Bank Group’s social, legal and environmental safeguards when entering into Public Private Partnerships to ensure:

- **the model is optimal for the outcome sought;**
- **in-country stakeholders are consulted closely;**
- **there is technology transfer and local capacity building included in contracts; and**
- **the partner government has, or is supported to develop, appropriate and transparent legal and regulatory mechanisms so they can fully participate, and any corruption is identified and addressed.**

PPPs for healthcare

- 7.48 Bupa, which operates a PPP in Spain observed that ‘Healthcare PPPs are often characterised by public funding, public control, public ownerships and private management’, and suggested that:

A public-private partnership to deliver health and care services in developing countries can represent a number of benefits to the host country. In many instances, developing countries are faced with a plethora of issues in need of being addressed yet have little

50 DFAT, Infrastructure, <www.dfat.gov.au/aid/topics/investment-priorities/infrastructure-trade-facilitation-international-competitiveness/infrastructure/Pages/infrastructure.aspx> viewed 1 April 2015.

funding and in many cases lack the skilled labour to meet these needs.⁵¹

- 7.49 However, others have raised concerns around the suitability of PPP models to deliver healthcare. Oxfam Australia restated a now infamous PPP arrangement which replaced a tertiary care hospital in Lesotho, which had led to significant cost overruns, with its Government ‘locked into an 18-year contract that is diverting scarce public funds from primary healthcare services in rural areas, where three-quarters of the population live.’ Oxfam contended that:

Lesotho’s experience supports international evidence that health PPPs of this kind are high risk and costly, and fail to advance the goal of universal and equitable health coverage.⁵²

- 7.50 Also referring to the Lesotho example, Abt JTA suggested that while there have been concerns about which health issues governments should address, the PPP model itself showed positive results:

...there has been an independent evaluation of the Lesotho hospital, showing some very positive outcomes ... I think it is fair to say that some NGOs and others are disputing the reasonableness of the amount of money that has been spent on a tertiary referral hospital and the lack of investment in the rest of the services, there is no doubt – I think the evidence stands – that the hospital is providing more services, higher-quality services, better-quality staff and a better outcome for a tertiary referral hospital.⁵³

Attracting the private sector to infrastructure PPPs

- 7.51 The then B20 Sherpa, Mr Milliner, highlighted the pressing need to attract private funding for infrastructure:

There is a very big deficit on infrastructure spending. Depending on how you assess it, there is a \$20 trillion or \$30 trillion gap between the capability of current governments to fund what needs to be done by about 2030. It needs to come from the private sector.⁵⁴

- 7.52 Private investors of all types – institutional investors and impact investors – are interested in funding infrastructure in the region. Impact

51 Bupa, *Submission 115*, pp. 3-4.

52 Oxfam Australia, *Submission 72*, p. 23.

53 Dr Jane Thomason, Chief Executive Officer, Abt JTA Pty Ltd, *Committee Hansard*, Brisbane 11 August 2014, p. 22.

54 Mr Robert Milliner, B20 Sherpa, B20 Australia, *Committee Hansard*, Canberra, 18 June 2014, p. 6.

Investing Australia observed that ‘areas like energy have a great track record and a number of people actually working in them’.⁵⁵ Impact Investing Australia also noted that diaspora communities are investing in sovereign bonds and infrastructure projects.⁵⁶

7.53 With respect to institutional investors, the ADB observed:

Both international and emerging market domestic institutional investors represent significant potential sources of capital that seek long-term infrastructure investment in developing economies. Theoretically the match is a good one; PPPs can offer institutional investors’ investment options in the current low interest rate environment and provide investors with a relatively predictable (inflation adjusted) cash flow. Coupled with banks’ long-term lending restricted by regulatory requirements, non-traditional lenders such as insurers and pension funds are poised to take a larger share of the long-term infrastructure investment (PPP) pie.⁵⁷

7.54 DFAT observed that ‘ODA is being used more actively to crowd in or leverage increased privately financed investment.’⁵⁸ It suggested that:

A constraint to greater private investment in areas such as infrastructure is the cost (time and money) of project preparation and the lack of ‘investor ready’ projects. To address this, many donors provide grant funding for project preparation in an attempt to provide information to investors on the financial viability of projects.⁵⁹

7.55 In addition to project preparation, Complex Program Group stated:

Whilst equity is often available, there is a significant shortage of available debt finance in developing countries. Project bonds guaranteed by MDBs or government aid agencies so as to increase project credit ratings to investment grade can viably increase the availability of finance.⁶⁰

7.56 Adam Smith International noted that barriers to entry for private investors in infrastructure can be overcome:

The barriers to entry for private capital can be low-cost. Often the issues revolve around insufficient rates of risk-adjusted return for

55 Mrs Rosemary Addis, Co-founder and Executive Chair, Impact Investing Australia, *Committee Hansard Melbourne*, 15 August 2014, p. 40.

56 Impact Investing Australia, *Submission 66*, pp. 9-10.

57 ADB, *Submission 120*, pp. 2-3.

58 DFAT, *Submission 21*, p. 17.

59 DFAT, *Submission 21*, p. 44.

60 Complex Program Group, *Submission 154*, p. 2.

investors. Support can be effective when it helps governments instate a coherent framework that addresses these issues: fiscal incentives for market entrants; guarantee facilities to share commercial and sovereign risks; output based contracts for maintenance and operation. Such mechanisms provided by governments within a supportive regulatory and policy framework can overcome the barriers to investment, unleashing the investment power of the private sector.⁶¹

7.57 DFAT highlighted some of the ways in which the Australian Government, often through multi-donor facilities, is supporting private investment in infrastructure in the region:

- The Public-Private Infrastructure Advisory Facility (PPIAF) is a multi-donor fund that provides technical assistance to governments in developing countries. This allows them to implement the necessary policies, laws, regulations and develop effective institutions and government capacity that supports an enabling environment conducive to private investment. It also supports governments to develop specific infrastructure projects with private sector participation.⁶²
- The Water and Sanitation Partnership is a multi-donor partnership that supports poor people access affordable, safe and sustainable water and sanitation services. It works in 25 developing countries with national and sub-national governments. The domestic private sector is increasingly important in the supply of water and sanitation services as they often provide wider, more cost effective access, particularly to the poorest in peri-urban, small towns and rural areas.⁶³
- The Private Infrastructure Development Group (PIDG) is a multi-donor organisation which encourages private infrastructure investments in developing countries to enhance economic growth and poverty reduction. The PIDG operates globally through a number of donor-owned, project development companies. InfraCo Asia Development (IAD), one such facility, operates across East Asia as a project developer, funding early stage, high risk investments by taking an equity stake in projects. It develops projects that would not attract private sector financing because of high levels of risk. Once projects are developed/proven they will be sold to private investors.⁶⁴

61 Adam Smith International, *Submission 17*, p. 4.

62 DFAT, *Submission 21*, p. 51.

63 DFAT, *Submission 21*, p. 51.

64 DFAT, *Submission 21*, p. 51.

- Supporting the preparation and transaction of individual public-private partnership projects to best-practice standards, for example through the Philippines PPP Project Development and Monitoring Facility.⁶⁵

7.58 Mr Daniel Runde from the Center for Strategic and International Studies suggested Australia could become the donor of choice in support of the region's energy and infrastructure needs:

Australia should also support ...energy strategies and large infrastructure projects by providing finance, risk sharing and advice to governments to enable the full spectrum of energy and road infrastructure projects favored by developing countries...Supporting the energy needs of the developing world will require that Australia establish development finance capability similar to the U.S. Overseas Private Investment Corporation (OPIC) and USAID's Development Credit Authority.⁶⁶

7.59 DFAT further noted that in addition to financing solutions provided through PIDG:

A number of proposed infrastructure financing facilities such as the Global Infrastructure Facility (World Bank) and the ASEAN Infrastructure Fund (partnership between ADB and ASEAN) plan to use equity investments from the public sector to raise debt finance through bond issuance.⁶⁷

7.60 In November 2014, G20 Leaders agreed to establish the Global Infrastructure Hub – a knowledge sharing network with a four year mandate, to be located in Sydney:

The Hub will work to address data gaps, lower barriers to investment, increase the availability of investment-ready projects, help match potential investors with projects and improve policy delivery.⁶⁸

7.61 The Committee found the Global Infrastructure Hub to be a valuable initiative to improve the quality of infrastructure investments, ensure a project pipeline, and harness the collective expertise of stakeholders,

65 DFAT, *Submission 21*, p. 39.

66 Mr Daniel Runde, William A Schreyer Chair in Global Analysis, and Director, Project on Prosperity and Development, Center for Strategic and International Studies (CSIS), *Committee Hansard*, Canberra, 2 October 2014, p. 2; and CSIS, *Submission 136*, p. 2.

67 DFAT, *Submission 21*, p. 46.

68 Global Infrastructure Hub, 'Fact Sheet', <www.globalinfrastructurehub.org/files/2015/03/Global-Infrastructure-Hub-fact-sheet-20150305.pdf>, viewed 7 May 2015.

including governments and the private sector. The Committee notes the work underway by the Australian Government to implement the initiative, and encourages efforts to expedite the Hub's establishment and operation.⁶⁹

- 7.62 Further, the Committee understands that DFAT is in the process of developing an infrastructure strategy. The Committee encourages DFAT to address issues raised in the evidence, particularly in relation to:
- public sector capacity to implement PPPs; and
 - the need to ensure transparency and proper consultation with the developing nation governments, capacity building to allow for genuine partnering through good governance, technology transfer and training.
- 7.63 In addition, DFAT processes and guidance should ensure that the necessary specialist skills can be attracted to aid projects and safeguards policies are in place and implemented.

69 The Hon Joe Hockey MP, Treasurer, 'Support builds for the Global Infrastructure Hub', *Media release*, <www.joehockey.com/media/media-releases/details.aspx?r=471>, viewed 21 May 2015.

Recommendation 19

The Committee recommends that the Australian Government support and participate in Public Private Partnerships (PPPs), where found to be effective, to address social and other infrastructure needs in the Indo-Pacific region, ensuring that the Department of Foreign Affairs and Trade:

- explore and encourage all opportunities to leverage Australian business expertise and participation in the financing and provision of infrastructure in developing countries in our region;
- engage with the business sector early and comprehensively to share information about opportunities;
- continue targeted public sector capacity building initiatives for recipient governments in relation to PPPs;
- ensure safeguards policies are implemented by all partners; and
- review and amend the Adviser Remuneration Framework to ensure that the necessary specialist skills can be attracted.

- 7.64 While acknowledging the good work underway, the Committee reminds DFAT of the need to promote its expertise and initiatives, including by:
- ensuring all donor recipient countries are familiar with both PIDG and PPIAF; and
 - running regular forums where successful PPPs can be showcased.

Private provision of infrastructure

- 7.65 Adam Smith International observed that to reach the rural poor may require other approaches than large-scale PPPs:

The need for project finance and bankability places a focus on large pieces of infrastructure where transaction costs are proportionately low. This in turn tends to favour network infrastructure in urban or peri-urban areas. The financing challenge is far greater in the case of distributed or off-grid infrastructure. This leaves a critical gap in service delivery for the rural poor. Attracting private sector investment in infrastructure

for the rural poor is significant, and calls for an entirely different approach.⁷⁰

- 7.66 DFAT noted that, for example in the water, sanitation and healthcare sectors, governments or donors may offer subsidies ‘to encourage private sector providers to provide services to the poor, who are unable to pay the full costs of connection or use.’⁷¹ DFAT also observed that:

These take the form of results based payments such as co-payments, user fees, advance market commitments/floor prices or feed-in tariffs... subsidies are used to enhance the private return of investments where the public or social good outweighs the financial return to the private investors.⁷²

- 7.67 However, the Foundation for Development Cooperation observed that high amounts of aid or concessional finance may reduce the incentives for private investment in infrastructure:

Rather than Pacific governments approaching donors to fund energy infrastructure, the same funds could be directed to reduce risk, increase the capacity, or accelerate the roll-out of energy supply by leveraging available commercial finance and/or funding packaged by private sector infrastructure suppliers.⁷³

- 7.68 To address the significant infrastructure needs, entrepreneurs and the private sector are designing and implementing innovative solutions. For example, in the water and sanitation sector in Mozambique:

[The Australian Government] has provided support to train local entrepreneurs to supply sanitation services in small towns in the Nampula Province. Training sanitation entrepreneurs helps to address capacity constraints of local governments in small towns, allowing the local private sector to supply sanitation services.⁷⁴

- 7.69 Business for Millennium Development and Opportunity International both discussed an innovative Australian social business – Barefoot Power – which is providing lighting solutions aimed at the two billion people who do not have access to grid electricity. Opportunity International noted that Barefoot Power had created products specifically designed to meet the needs of weavers and that Opportunity International

70 Adam Smith International, *Submission 17*, p. 4.

71 DFAT, *Submission 21*, p. 44.

72 DFAT, *Submission 21*, p. 44.

73 Foundation for Development Cooperation, *Submission 78*, pp. 6-7.

74 DFAT, *Submission 21*, p. 50.

was working with its microfinance institutions to develop loan products that enable families to purchase those products.⁷⁵

7.70 The World Bank Group also provided an example of innovation by the private sector in Papua New Guinea, expanding accessibility to technology, and helping to improve safety and security:

...with US\$1.5 million in Pacific Partnership support, telecommunications company Digicel has designed solar-powered mobile charging stations for rural PNG which could allow 500,000 people who are not on the electricity grid to charge and use mobile phones for connectivity and trade. The solar systems have been designed to also provide street lighting to rural areas of PNG, improving security in the high-crime country, and are expected to provide income for approximately 500 new solar entrepreneurs by 2015.⁷⁶

7.71 Clearly innovation through private sector investment is the key to success in many cases. The Committee believes that the Australian Government's new innovationXchange, housed within DFAT, provides an opportunity to explore new solutions to intractable infrastructure challenges.

75 Business for Millennium Development, *Submission 93, 'Landscape Study'*, p. 50; Opportunity International, *Submission 76*, p. 18.

76 World Bank Group, *Submission 75*, p. 20.