

POTENTIAL FOR PUBLIC PRIVATE PARTNERSHIPS IN AFGHANISTAN

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I. RELEVANCE AND IMPORTANCE OF PUBLIC- PRIVATE PARTNERSHIPS FOR POST-CONFLICT COUNTRIES

A number of factors common to many post-conflict countries such as Afghanistan make the concept of public-private partnerships for the delivery of public services particularly relevant:

- ◆ People in countries emerging from conflict typically face **increased needs** for basic infrastructure, due to (i) disruption of services or destruction of existing assets, and (ii) limited or no development of new projects during the conflict.
- ◆ At the same time, these countries' **public and private sectors lack adequate resources**, both financially and in terms of skills, to re-establish these services quickly. Therefore, many post-conflict countries turn to international donors and private investors for resources.
- ◆ **International private investors are reluctant** to expose themselves to excessive country risk by investing before there is a clear path to a stable investment climate – both in terms of security and a steady economic setting.
- ◆ The public sectors are typically constrained by **weak absorptive capacity**. At the same time, policy priorities in the initial period may dictate a focus on aspects other than establishing the necessary investment climate to spark the interest of potential private investors in areas of public interest.
- ◆ Therefore, there is often a “**bitter paradox**” in the first few years of reconstruction – governments can neither absorb reconstruction aid nor attract much private investment to offset the Government’s low absorptive capacity.

While it is important to point out that PPPs cannot be the solution for every challenge that the public sector faces in delivering infrastructure or services, they can help alleviate or even overcome some of the previously listed problems when the right environment and support structures are put in place.

What is a Public-Private Partnership?

The concept of public-private partnerships (PPPs) is not new, with PPPs taking on a variety of forms. These partnerships basically involve various aspects of private initiative working with the public sector in a relationship that entails reciprocal obligations and mutual accountability, including either voluntary or contractual ties; sharing of investment and risks; and joint responsibility in planning, design and implementation. PPPs allow government to transition from managing and providing services, to enabling and regulating private initiative which delivers the services.

More specifically:

PPPs are used for products and services that are considered to be a universal service to the population. They do not usually cover industrial or commercial activity that is routinely undertaken by the private sector on a “market” basis.

The basic principle at the heart of a PPP is that the relevant risks should be allocated to the party that is best able to absorb or mitigate them – some risks will stay with the public sector, and that fair allocation of risks requires commensurate allocation of rewards.

The degree of private sector involvement and risk sharing can vary enormously depending on a number of factors. The scope of involvement can range from (a) limited “outsourcing” contracts for the provision of technical or management services by the private sector to (b) full scale operating concessions and/or partial privatisation.

Typically PPP projects are classed in two main categories:

- **Economic infrastructure.** Services for which sustainable levels of revenue can be derived to pay for investments, operations and risk-related rewards. For such projects, the private sector may be prepared to take all or a substantial portion of the market/revenue risk. Prime examples typically include toll roads and other transport projects, power generation, water treatment concessions and telephone services.
- **Social infrastructure.** Projects for which it is not feasible or inappropriate to expect users to pay all aspects of the actual cost of the services necessary for the private sector to take market/revenue risk, but where private sector operation and management expertise and risk sharing is seen as beneficial. Typical examples include hospitals, schools, government accommodation, and water and electricity distribution.

The main benefits of PPPs include:

- ◆ By bringing the private sector into certain portions of infrastructure, the **government can leverage its own budgets**, increasing the amount of infrastructure that can be developed with a limited budget while allowing government to concentrate on the social infrastructure and other social spending that is not of interest to the private sector.

The potential size of private sector investment in public services infrastructure is illustrated by the World Bank estimate that since 1990, the transfer of operating risk of power, water, telecommunications and transport projects to the private sector (through a wide range of PPPs in over 130 developing countries) has resulted in the mobilisation of about US\$750 billion in investment commitments.¹

- ◆ PPPs allow for a combination of public sector administration and oversight whilst harnessing the strengths of the private sector in the provision of goods and services. Public service provision can therefore **benefit from private sector strengths** in the areas of, for example, cost-benefit analysis, financing, expertise, innovation, speed, flexibility and management.

- ◆ PPPs provide the benefits of **genuine risk transfer** to the private sector. This translates into less uncertainty about future expenditure, relief from budgetary constraints, and the freeing up of management capacity within government.

Depending on the exact form and scope of the particular PPP, this includes key project risks such as:

Construction (risks of cost, specification and timing of completion all tend to lie with the private sector in PPPs)

Operations (most technical operating risk – i.e. meeting certain specified outputs with penalties for failure to perform – typically lie with the private sector in a PPP)

Revenue risk (the extent to which this risk might lie with the public sector, the private sector, or might be shared between them, will depend upon the particular strengths of the project and the appetite for such risk within the private sector)
Other risks including interest rate risk, macro economic risks, forces majeures (“acts of God” such as floods or earthquakes) and political risks (including riots and terrorism) tend to lie most naturally with the public sector

II. PPPS IN POST-CONFLICT COUNTRIES (PCC): THE CHALLENGES

The previous section has discussed the potential benefits that a country can derive from applying the PPP concept to the provision of parts of its public services. However, a number of conditions must be met for public private partnerships to be able to yield the desired results. Particularly in developing, and even more so in post-conflict countries, these conditions are often not or only partially met.

Problems are particularly related to the following three areas:

- ◆ **Weak institutional and legal structures** can substantially increase the cost of putting PPPs together
- ◆ **A low ability and willingness of consumers to pay for or of government to subsidise** increases revenue risk and lowers project viability
- ◆ Due to the **higher perceived risks of investing** in a PCC, the required returns for the private sector are higher than in politically stable environments

The combination of these three factors can result in a project “viability gap”, leaving only the very best projects feasible. Therefore, adoption of PPP models in developing (and post-conflict) countries is particularly challenging (which explains why so far very little has been done).

The key challenges include a lack of:

Requisite laws

There is a need for a body of legislation relevant to PPPs, and the effective and even-handed enforcement of such laws. Key laws that are required typically include laws that:

- ◆ Allow the public sector to procure goods and services from and cede interests in infrastructure on a long-term basis to the private sector (sometimes existing legislation can be adapted to allow this, other times new PPP laws need to be enacted or bilateral contracts are used as the basis for discrete PPP initiatives or in advance of wider legislation)
- ◆ Govern ownership, mortgaging / monetisation and foreclosure of land and other assets. This needs to address not only domestic concerns, but also develop the necessary legal basis for non-domestic companies to own, dispose of and operate assets. For example, for international bidding to be successful, the international partner will want to exert a certain level of control over the venture

- ◆ Allow for effective and efficient dispute resolution
- ◆ Pertain to bankruptcy, accounting, etc. and other general aspects of doing business

Government understanding and capacity to implement and oversee PPPs

Both as a contract party and as a PPP initiator, the government needs to have the capacity and capability to undertake PPPs. This includes the ability to:

- ◆ Select projects for PPP procurement
- ◆ Undertake some initial due diligence and feasibility studies to determine appropriateness for the PPP and the optimal PPP structure
- ◆ Prepare a bidding process to include short-listing criteria and process, preparation of bid instructions, preparation of PPP contract forms, dissemination of information, bid evaluation, and process of selection and award
- ◆ Negotiate the terms of the PPP with the awarded concessionaire
- ◆ Oversee the PPP implementation
- ◆ Stand by the government’s obligations under the PPP

Managing this competitive process in a value-maximising way is an enormous challenge for the public sector. Even the most experienced governments tend to recognise their own limitations and call upon experts (technical, legal, financial etc.) to assist in this process.

One way to address management issues is to establish dedicated PPP units within central government (typically at the Ministry of Finance level) and often also within line ministries and other relevant government departments to manage the PPP process, amend and disseminate policy, spread best practice and publicise lessons learnt.

As just one of many examples, in 1999 the Netherlands established the PPP Knowledge Centre (within the Ministry of Finance) which is staffed with experts from the private sector and from Government. It has the job of making the PPP experience known to participants, designing clear rules and templates for PPP identification and procurement. It also outlines the rules governing the interaction between the public and private sectors, suggests appropriate projects for PPPs, and

produces studies and reports on PPPs including lessons learnt and best practice recommendations.

Requisite transparency to ensure that PPPs are procured in an open and value-maximising way

The key to fostering successful PPPs – that deliver the expected long-term benefits in terms of service and asset provision – is competition. Only by fostering and managing a truly open, competitive and fair tendering process for PPPs will the desired outcomes be met.

Government financial capacity (and/or creditworthiness) to share revenue or other financial risks in a PPP

Post-conflict governments, including the Government of Afghanistan, will often not be able to shoulder their share of the financial risks involved in PPP projects without the backing of international donors or credit institutions.

Government track record in terms of honouring contracts and performing under a PPP

All PPPs rely on contracts between the public sector and the private sector. The private sector needs to be comfortable with all underlying aspects of both a particular project as well as the underlying relationship with its partner, the government. This particularly involves:

- ◆ Consistent long-term commitment on the part of the government to implement and stand behind PPP policy and projects
- ◆ The recognition that the private sector should be allowed to earn adequate returns to compensate it for the risk taking
- ◆ The private sector having reasonable certainty that it would be able to implement the PPP on the agreed basis free of interference once the PPP was awarded
- ◆ The private sector being confident that the laws would be fairly and consistently applied, and more importantly, that it would have redress against the government itself should the government fail to honour its contractual obligations

Local private sector expertise and ability to absorb the risks associated with a PPP

A common constraint is the lack of interest and capability within the domestic private sector to competitively bid for PPPs, and then to manage them for the term of the contract. Experience shows that it can take considerable time for the domestic private sector to build up the capability, capacity and appetite for PPP project bidding and implementation.

International private sector interest in the country

In countries such as Afghanistan, international investor interest is often weak or limited to a few key sectors and/or the expatriate community.

- ◆ There needs to be “buy-in” for PPPs from the government, the private sector and from the ultimate beneficiaries: the public
- ◆ There also needs to be assurance of no renewed conflict or disturbance to economic activities

For the above to be sustainable, given the long-term nature of PPP investments, there needs to be a reasonable level of political and economic stability.

III. HOW TO MAKE PPPS WORK IN POST-CONFLICT COUNTRIES

Despite all these challenges, experience has shown that public-private partnerships can work in post-conflict environments and that they have the potential to contribute to the efficient and sustainable delivery of public services over time. A report from the Commonwealth Secretariat² found that: “Experience to date suggests that the potential for PPPs in infrastructure, that is, for the private sector to assume a degree of risk in investing in and/or delivering a service, will increase over time and with the onset of greater stability – even though this can be a slow and not necessarily a linear process.”

In what sectors are PPPs most likely to be successful

In post-conflict countries, initial PPPs tend to come in the most commercially viable sectors where little government support is required and particularly where foreign currency revenues can be earned. The principal example would be

telecommunications, which tends to be one of the first sectors to take off (as has occurred in Afghanistan as well as in several African PCCs). **Natural resource extraction**, such as oil and gas or various metals, are also sectors ripe for early stage PPPs (this is particularly true in Afghanistan given its rich resource base) and given the established risk appetite of international oil and gas and mining companies for making investments in challenging environments worldwide.

Experience has shown that **transport** PPPs tend to take some time, and that the focus is usually on ports and airports with their ability to earn hard currency from international travellers/shippers and higher net worth consumers/companies. Purely domestic transport projects tend to be very challenging, not only in PCCs but in developing countries in general. Nevertheless, oftentimes local communities show a willingness to get together and provide the required service, with a minimum of government oversight and support.

In **power**, the experience has been that it takes many years after stabilisation (six to seven according to the Commonwealth Secretariat report) for PPPs to be feasible – and then only in power generation.

In **water and sanitation** even more time is generally required, and the examples of PPPs in post-conflict countries are few. Even in developing countries, typically PPP structures tend to be of the shorter/simpler variety.

In Africa, **electricity and rail transport** have accounted for over half of the limited volume of PPPs. However, this is unlikely to be initially applicable to Afghanistan due to the lack of existing infrastructure – the management of which was the driving force behind many of the African examples.

Specific considerations for PPPs for social infrastructure

A key difference to economic infrastructure is that typically for social infrastructure projects, expecting users to pay all aspects of the actual cost of the services necessary for the private sector to take market and revenue risk is politically not feasible or inappropriate from a social perspective (this also applies to projects in or projects to remote parts of the country, but which may have been sustainable in an urban setting). At the same time, the services are seen as essential and merit early focus in the rebuilding process. This, coupled with the constraints on subsidies from the government,

make PPPs a delivery mechanism worth considering.

Key sectors where social sector PPPs can be useful include **health, education and cultural heritage**.

Social sector PPPs can also act as **pilot projects**, where the government and private sector gain experience in delivering services in partnership. Often, this role can be played by NGOs. In Afghanistan's health sector, for example, the bulk of public health expertise resides in the NGO community.³

Some of the aspects of working with non-profit NGOs include:

- ◆ Just like other agents in the private sector, NGOs can be more flexible than government (e.g. in the recruitment of staff) and also be more innovative.
- ◆ Non-profit NGOs are able to work with lower return requirements compared with for-profit companies. This is particularly useful in the “bitter paradox” situation described in Part 1, and can be a first step toward demonstrating sustainable funding modes when standard PPPs are initially less feasible.
- ◆ It is important, however, to look at the long-term sustainability of the services. As demand grows, so can the expectation of free or subsidised service delivery, and mechanisms must be in place to cater to this need. Some NGOs (the larger international organisations) may supplement contract funds with their own resources. In others, a path to sustainability with increasing rates may be considered.
- ◆ Mechanisms for interaction between government and the not-for-profit sector can reinforce constructive dialogue.

Just as in economic infrastructure, contracting needs to be competitive to encourage providers to maintain efficiency and quality. Likewise, contract specification and implementation monitoring need to be addressed, with the cost of monitoring linked to government capacity to carry out the stewardship.

How to maximise the potential of PPPs in post-conflict countries

Given (i) viability gap issues, (ii) the discrepancy between what the private sector expects and what the government can deliver and/or the public can afford, (iii) the paucity of rules and regulations and (iv) the lack of credibility of local governments as a

contracting counterparty, PPPs will necessarily be highly dependent on support from outside agencies, including the various donor agencies (MDBs).

To allow PPPs to happen, donor agencies will need to help with:

- ◆ Design
- ◆ Procurement
- ◆ Provision of significant credit enhancement (essentially guaranteeing or backing up the government's obligations) and/or subsidies

There are many examples of this kind of support from donors even in more developed markets:

- ◆ WB and ADB provide guarantees to backstop the obligations of the Government in the sale of the national electricity transmission company in the Philippines
- ◆ The provision of subsidies by various donor agencies to allow the Pamir Power Project to happen in Tajikistan

There is also a need to **think small** – to look at PPPs on a local community scale. An example would be the provision of power solutions at a local/rural level with the involvement of local participants/ entrepreneurs – typically this would involve a simplified form of PPP with fast-tracking and might involve participation by NGOs.

The lack of government capacity can also be seen as an opportunity – **many aspects of government service are suitable** for private sector contracting or outsourcing. This can be anything from civil servant payroll management, to catering, to processing of passports or other statutory documents, to provision of new buildings and training. All of these can be possible subjects of PPPs. The key is to start with the ministries or government agencies that are most open to private sector contracting, and start a few pilot projects which can then expand across services and different areas of government.

Use investment opportunities in **tradable sectors** to mobilise investments in infrastructure (business licence + obligation for service provision).⁴

Initially contracts may be **shorter-term**, to enable sector planners to learn and incorporate changes to future PPP structures, and to the Government's own organisation and strategic direction.

Don't expect too much: private infrastructure in the low-income markets is taking off slowly.

Be flexible and creative: Look for opportunities that may not fit the traditional definition of a PPP – anything that harnesses private sector expertise and financing to help provide or support public services.

Case Study 1: Creative interim solutions to encouraging private sector involvement in the provision of basic services to the public (Cambodia)

A common occurrence in conflict and post-conflict countries is the emergence of unregulated, small-scale private providers of infrastructure, particularly in electricity and water supply.

Because small-scale private service providers evolve as a response to the lack of government, they are generally unlicensed, unregulated and often targeted as nuisances by the public utilities that are trying to reinstate their exclusivity rights.

The quality of services provided by these private companies is often low, while prices are high. However, the real alternative available to the rural and peri-urban communities in many conflict affected countries is not a world-class investor or even a struggling state-owned utility – it is no service whatsoever.

Despite their shortcomings, these small-scale private companies often provide vital services to communities that cannot be reached in the short to medium-term by the State.

In recognition of this role, post-conflict countries as varied as Mozambique, Sri Lanka, El Salvador and Cambodia are now introducing regulatory arrangements that recognise private providers; encourage efficiencies through associations, mergers and convergence; and introduce minimal levels of oversight to alleviate extreme cases of rent seeking and quality of service deficiencies.

*Cambodia: Small-scale provision as an interim solution to service delivery*⁵

It is estimated that between 600 and 1,000 small private power systems are operating in Cambodia, serving about half a million customers (or nearly as many households as the national power company). Most of these entrepreneurs set up their businesses prior to the formation of the interim Government in the mid-1990s and continue to provide services to communities who otherwise would have no network connections. In their totality, these small independent companies have about half of the country's generating capacity. The majority meter their customers and charge either a flat rate or a

single block decreasing tariff. They average 200 households per business. In recognition of their importance, the country's Rural Electrification Strategy – supported by the donor community – envisions the convergence of these small power providers into local distribution companies as transmission is rolled out across the country.

Private companies that treat and deliver water through piped and metered systems can also be found throughout the Cambodian countryside, albeit with much less frequency than the mini-power companies. These water companies were built almost entirely with local equity and offer a service desperately needed by villages and peri-urban communities. Recognising the importance of these providers, recent donor activity in Cambodia has attempted to encourage their spread throughout the provinces through targeted subsidy incentives and Design Build Lease contracts that reduce investment risk.

Conclusion

The example provides important lessons for the Afghan context, particularly for the provision of electricity and water to rural populations in remote areas that will not receive government services in the foreseeable future.

Case Study 2: Pamir Energy, Tajikistan: Donor support ensures social protection within a PPP for power generation in a post-conflict setting

With the collapse of the former Soviet Union, conditions in the mountainous eastern Pamir region of Tajikistan deteriorated dramatically. Electricity infrastructure quickly fell into an advanced state of disrepair and power plants and many distribution lines were destroyed during the civil war in 1992. The ensuing sharp economic decline (GDP contracted by 60 percent) and neglect by the national electrical utility left 43 percent of homes in the region without power during the harsh winters, where temperatures reach -30°C. Schools, health centres and small businesses were forced to close in cold winter months stifling economic and human development. With many people forced to use wood for cooking and heating, 70 percent of the region's sparse forest cover was lost. Smoke inhalation from indoor wood fires led to a sharp increase in respiratory disorders.

At that time, Tajikistan's estimated per capita income was around US\$ 160/year and 60 to 80 percent of people were living below the poverty line and relying on subsistence agriculture. Those that did have access to electricity were used to

paying 0.4¢ per kW/h, less than one-tenth of the production cost. Under these conditions, attracting private sector investment into the energy sector with traditional approaches would have been difficult at best.

The **PamirEnergy** Company, jointly owned by AKFED and IFC, with equity of 70 percent and 30 percent respectively, was established in 2002. AKFED has invested US\$ 8 million in equity and the IFC has committed US\$ 3.5 million in equity and US\$ 4.5 million as debt. PamirEnergy operates under a 25-year concession contract to operate the electrical utility assets in the Pamir region, improve transmission infrastructure and hydro generation capacity, and regulate the level of Lake Yashilkul to ensure adequate water flows in winter. PamirEnergy also assumed responsibility for the utility's 30,000 existing customers and 595 employees.

The PamirEnergy project demonstrates an **innovative public-private approach** in overcoming a number of challenges, including the limited ability of customers to pay for electricity services. The project has pioneered a new way of collaborating between investors, development agencies, bilateral donors, governments and the project sponsor.

A key aspect of the project is the social protection scheme that ensures that tariffs paid by households remain affordable, while the tariffs received by the investors provide a rate of return commensurate with the risks involved in such a project.

The World Bank's International Development Agency (IDA) loaned US\$ 10 million to the Government of Tajikistan at a rate of 0.75 percent. These funds are on-lent to Pamir Energy at 6.00 percent, allowing PamirEnergy to partially finance its capital investments at less than commercial terms and pass these savings on to customers as lower tariff rates. This 5.25 percent lending margin, plus a US\$ 5 million grant by the Swiss Government to the Government of Tajikistan, has been used to finance a tariff subsidy to ensure that a "lifeline" monthly supply of electricity is delivered at a very low rate even to the poorest of households. Also built into the tariff structure is an "Early Years Subsidy" – a long initial grace period that allows tariffs to climb slowly from current levels – thus further reducing risk and keeping tariffs affordable.

Lessons for Afghanistan

- ◆ Attracting private investment for the provision of infrastructure services is possible, even in high-risk contexts, provided the involvement of an MFI from an early stage.

- ◆ Innovative combinations of international grant aid with preferential loans can at the same time ensure social protection for customers and acceptable rates of return for the private investor.

IV. PPPS IN AFGHANISTAN: EARLY SUCCESSES

Afghanistan is seeing **strong market-based** private sector entrepreneurial activity at the very small-scale end of business, but enormous impediments remain to scale such efforts up to higher levels. Much medium-scale activity is geared to donor funded construction or toward consumer goods (e.g. Coca Cola bottling plant, trading in tea, cigarettes, fuel products, etc.), but not yet toward long-term service delivery.

Afghanistan's positive policy stance on private sector investment is very encouraging (e.g. through AISA), but while several key pieces of legislation have been passed or are being tabled, **enormous concerns remain** regarding the legal and regulatory environment, especially with respect to:

- ◆ The transparency process, including the role of ministries vs. regulators
- ◆ The future stability of recently implemented legal and regulatory frameworks

Nevertheless, some clear successes in terms of private sector involvement in quasi-PPPs have already demonstrated viability under the right conditions:

- ◆ Telecoms - licence awards for cellular telephony
- ◆ Well-regulated banking sector has attracted investment and is now competitive and thriving although still on a minute scale. The rudiments of a microfinance climate are also emerging

Some other sectors are opening up for private sector investment:

- ◆ Oil and Gas, Mining – awards of exploration and refining licences ongoing
- ◆ Fuel Products – more on a private sector basis than through PPPs
- ◆ Cement – a good example of a “licence” structure, where the winning bidder undertakes to maintain certain social obligations (e.g. retention of staff and provision of excess electricity to the grid)

The GoA is already implementing a number of **very successful large-scale social infrastructure**

programmes within PPP-similar arrangements in the health sector (Basic Package of Health Services, BPHS) and in rural development (the National Solidarity Program, NSP). Both are implemented in partnership with the not-for-profit national and international NGO sector.

Many issues remain before a vibrant PPP market can emerge. Some of the more basic **building blocks that are still lacking** include corporate bank lending with longer tenors and larger amounts (and in the medium to long run, corporate bond markets); commercial insurance; land use and titling systems; a reliable judicial system, including enforcement of awards; as well as foreign investor appetite due to a worsening security situation.

In addition, the typical PCC institutional gaps discussed in Part II also apply to Afghanistan:

- ◆ Government PPP understanding and processing capacity
- ◆ Local private sector capacity to undertake PPPs (including requisite skill sets within businesses to, for example, put together a business plan)

Case Study 3: Basic Package of Health Services (BPHS): The provision of social infrastructure – government and the non-profit sector working together

In 2002, Afghanistan had some of the worst basic health indicators in the world. Infant mortality was at 165 per 1,000 live births, there were 1,600 maternal deaths for every 100,000 births and over 25 percent of children were dying before their fifth birthday. The provision of health services to the population was characterised by low capacities and reach of MoPH facilities, with health service delivery effectively having been taken over by NGOs during conflict years. This resulted in the absence of effective quality controls, and uniform systems and standards across the country. Over 60 percent of the population had no access to any basic health services whatsoever.

The Basic Package of Health Services (BPHS) was developed to improve the dramatic health indicators of the country by:

- ◆ Ensuring access to basic health services for the entire population
- ◆ Unifying the health service delivery and bringing the existing extremely fragmented health activities back under government control

- ◆ Establishing consistent standards for the provision of basic health services

The main structures and mechanisms include:

- ◆ Government as a steward and owner of the public health system, but not directly involved in delivering basic health services
- ◆ Private health service providers (currently 27 national and international NGOs) implementing the BPHS through various contractual arrangements with the Ministry of Public Health
- ◆ Each NGO providing the services detailed in the BPHS including clear definitions of which staffing, equipment, diagnostic services and medication requirements have to be provided by various basic health facilities
- ◆ Communities as active partners through the provision of land and labour for constructing health facilities, the training of community-based health workers and the establishment of health committees
- ◆ 100 percent of the BPHS being currently donor funded. Donor agency grants are channelled through a grant unit within the MoPH. Contracts are allocated through competitive bidding

A major success of the BPHS since its inception in 2002 has been the considerable increase in the proportion of the population with basic access to BPHS services from under 40 percent to nearly 77 percent as of mid 2005. It has also brought coherence and unified the priorities of the Afghan health system, facilitated unambiguous decisions about the direction of the health system and standardised the classification of health facilities.

Key challenges of the approach relate to issues of financial sustainability, competition and the long-term role of Government in the delivery of basic health services:

- ◆ The BPHS is 100 percent donor funded and while the charging of user fees is allowed, the potential cost recovery from users, particularly in remoter/poorer areas, is low.
- ◆ Funding a large amount of the BPHS budget through government revenue is not realistic in the foreseeable future. Therefore, the question arises of what happens when donor fatigue sets in.
- ◆ Particularly for remoter parts of the country, competition for awarding contracts has been low. This will be even more the case for reaching the remaining 33 percent of the population. An

important factor for higher service delivery efficiency through the private sector might therefore not be given.

- ◆ There are reservations within Government about using NGOs for health service delivery in the long-run. This is connected to uncertainties about the long-term commitment of international NGOs on the one hand, and about Government seeing a chance of increasing its legitimacy through the direct provision of basic health services on the other.

Conclusion

- ◆ An effective way of using private not-for-profit sector expertise and infrastructure while ensuring government control and ownership, quality and systematic coverage of the population
- ◆ In the absence of strong competition, the long-term efficiency and performance of the system need to be monitored
- ◆ Experience gained in the process of negotiating and managing contracts with a large number of actors could be used for other PPP-type arrangements

V. RECOMMENDATIONS FOR THE DEVELOPMENT OF SUCCESSFUL PPPs IN AFGHANISTAN

In the words of a PPP policymaker at the EU Commission⁶: “PPP arrangements work best where there is an explicit policy commitment by national governments to involve the private sector, a clear long-term political will, a high-quality partnership, transparency, clearly specified financial guarantees and an established, stable legal environment.” Obviously, much of this is still missing in Afghanistan.

Some specific, practical observations on what can be done to start the PPP development process include:

Implement pilot projects

Gain experience in some pilot projects which have strong economic fundamentals and require minimum government intervention (“low-hanging fruit”), but where “lessons learnt” can be applied to other projects in the future:

- ◆ Create the enabling environment – including some model contracts
- ◆ Use lessons from overseas
- ◆ Ensure an open and transparent bidding exercise
- ◆ Have donors provide requisite credit/contractual support for the first PPPs and support in the overall PPP procurement process
- ◆ Harness the ability and resources of the NGOs

Also need to look at some small-scale PPPs on a fast-track basis at the local/rural level leveraging off microcredit. Look at providing service contracts for core government services back-stopped by IFIs, NGOs, etc.

Continue to improve the general business environment

Given the enormous challenges for PPPs in Afghanistan, the country has to go out of its way to create a friendly enabling environment and attractive terms of investment for the private sector. This is nevertheless covered elsewhere in the Conference and will not be elaborated upon here.

Further develop the regulatory framework

- ◆ Create truly independent regulators (such as TRAA) for key sectors
- ◆ Allow offshore arbitration or other neutral dispute resolution proceedings

Focus on government policy and capacity building

- ◆ GOA needs to make a clear commitment to PPPs as a part of private sector development – political leadership is essential
- ◆ Work to maximise government credibility as contract party – starting with the parts of government most amenable to change
- ◆ Build capacity (including a PPP unit) within the government (MOF) and key line ministries as and when needed in tandem with the pilot PPPs
- ◆ Start the medium-term capacity building to allow PPPs in core utility sectors such as power, water and transport, while recognising that immediate results are unlikely

Enlist the assistance of donors and multilateral finance institutions

- ◆ Have donor and specialist agencies (such as Partnerships UK and similar outfits around the world) provide capacity building support and resources for the Government to get PPP projects off the ground and to manage the process
- ◆ Use and expand the political risk guarantee facilities (such as AIGF – MIGA and ADB) to provide comfort for PPP investors and lenders
- ◆ Prompt donors to look at incorporating PPP elements into their public sector infrastructure programmes where this is at all feasible (but not over-promising as opportunities are initially likely to be limited)
- ◆ Have donor and specialist PPP agencies provide assistance to the private sector so that capacity can be built up for PPP investment (through a facility with AISA or a new PPP window which would act as an investor advisory service, helping investors to present bids, write business plans and undertake financial modelling, etc.)

Be realistic

There will be limited PPP opportunities, at least for some time, but if a handful of strong examples can be built up, then the market could eventually take off.

¹ World Bank, *The Investment Climate in Afghanistan: Exploiting Opportunities in an Uncertain Environment*, 2005, p.24.

² Harnessing Existing Financing Facilities to Promote Public-Private Partnership for Infrastructure Investment and Service Delivery in Post-Conflict Countries, Draft Final Report February 2005

³ Reference: Natasha Palmer, Lesley Strong, Abdul Wali and Egbert Sondorp, « Contracting out health services in fragile states, » *BMJ*, Volume 332, 25 March 2006.

⁴ Reference: Public Policy for the Private Sector: Rebuilding Infrastructure, WB Private Sector Development Vice Presidency, Note Number 306, March 2006.

⁵ (from: 'The Private Sector's Role in the Provision of Infrastructure in Post-Conflict Countries: Patterns and Policy Options' by Jordan Schwartz, Shelly Hahn, Ian Bannon, Social Development Papers, Conflict Prevention & Reconstruction, Paper No. 16/ August 2004)

⁶ Deputy DG of DG TREN, European Commission at the 2005 PPP Transport Summit