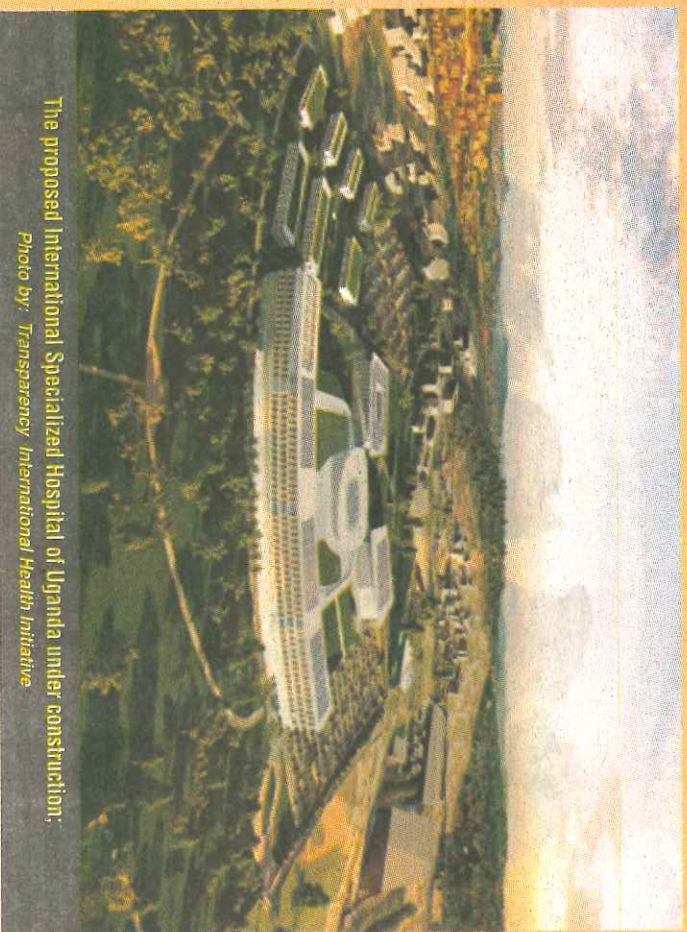




PUBLIC PRIVATE PARTNERSHIPS: AN EMERGING FORM OF HIDDEN DEBT WITHIN THE EAC?



The proposed International Specialized Hospital of Uganda under construction.
Photo by: Transparency International Health Initiative

Introduction: In Africa, many countries are currently facing a decline in public sector resources such as tax revenue, aid, among others which has constrained national budgets and the capacity of these governments to finance their development. To address this issue partly, Public-Private Partnerships (PPPs) have emerged as the magic bullet to leveraging private finance to fund development projects and public services, such as health, education, water and sanitation, transport, and energy services. PPPs are long-term contractual arrangements between the public and private sector for the provision of. PPPs are seen as a relevant instrument for delivering the Sustainable Development Goals (SDGs).

However, the adoption and implementation of PPPs by countries has not been flawless. International experience on implementing the PPP strategy reveals that in a number of cases, implementation of PPPs has had unintended consequences that have constrained local development. Among the observed unintended consequences of PPP projects are the following: cost escalation of goods and services delivered under the strategy, financial risks skewed to the government side, tendency of PPP projects to benefit some but not all intended beneficiaries, vulnerability to corruption and general lack of transparency of PPP projects, lack of people's voice at all levels of PPP project design and implementation, and putting little emphasis on long term environmental and socio concerns of communities. An example of the considerable financial risks involved is a large-scale road-building program in Mexico in the 1990s that involved more than 50 PPPs. Unanticipated costs and macroeconomic shocks led to the government bailing out over half of the PPPs and assuming close to \$8 billion in debt (UNCTAD, 'Trade and Development Report' (2014) 18.

This statement therefore seeks to explain the

inherent risks on fiscal sustainability that underlie PPPs and thus provoke debate on the need for an appropriate financing model to be embraced for all PPP projects within the East African Community (EAC) region.

The Genesis of PPPs

The PPP financing model is a solution that emerged years ago and has been viewed as an important way to help developing country governments to raise resources to finance the realization of development goals including the Sustainable Development Goals, among others.

The history of PPPs can be rooted in decisions that were made during the first International conference on Financing for Development in Mexico in 2002, in which the business community was for the first time invited to join in the discussions of the Monterrey Consensus, which they actively supported. In this consensus, a chapter was devoted to Foreign Direct Investments (FDI) and other private inflows as international resources for development. Developing countries as a compromise were given clear responsibilities that they were obligated to fulfill if they were to attract and enhance inflows of productive capital into their countries. The consensus also emphasized the need for these countries to achieve a transparent, stable and predictable investment and respect of property rights, with economic policies that promote and protect investments.

In 2004, PPPs emerged as the new form/category of blended finance. Due to tighter national budgets owing to numerous fiscal constraints in these countries and changes in the international aid architecture, PPPs are growing at a much faster rate than earlier anticipated. They are now being viewed as potential arrangements for mobilizing private capital to bridge the gap in public sector financing.

PPPs in the EAC

Within the EAC region, partner states' development plans underscore the role of the private sector in financing the country's development. They strongly promote PPPs and put forward a series of strategies to support a conducive environment for doing business. In addition, national legal and institutional frameworks to facilitate greater use of PPPs not only in infrastructure, energy and mineral development, but also in other sectors such as education and health have been developed. In support of these developments, a considerable body of information material has also been made available for these governments on good practice in PPPs, and international institutions such as the World Bank and several donor organizations are providing technical assistance and support to governments in the area of PPP projects.

Remarkably, according to data provided on the PPP Knowledge Lab, PPP projects in the EAC region are currently valued at \$2 billion in Uganda, \$851 million in Rwanda, \$5.1 billion in Kenya, \$16 million in Burundi and \$1.1 billion in Tanzania.

PPPs as a hidden debt

Critics of PPPs warn that a key driver for using PPPs in developing countries has been the urge to remain within the minimum debt to GDP ratio. They do this by adopting accounting practices that allow governments to keep the cost of the project and its contingent liabilities "off balance sheet". While at face value, this has been largely achieved, there is an ever growing concern that many African countries may soon fall into unsustainable debt levels given the tendency of PPP projects to cost twice as much, compared to if they were implemented directly by government.

Another concern with the PPP financing model stems from Governments guaranteeing loans acquired by the private actors through the use of instruments such as Promissory notes, losses incurred by the private sector during the project implementation, rates of return, minimum income streams, currency exchange rates, and compensation should new legislation affect an investment's profitability. All these are aimed at making the PPP projects look bankable. Consequently, risks associated with PPP projects are socialized while the profits are privatized, which beats the rationale behind PPPs of the public and private sector sharing risks. Cases of this nature can be seen in the February 2019, FINASIS/ROKO Construction Special Purpose Vehicle Limited in which the Government of Uganda issued Promissory Notes worth USD 379.71 Million for financing of the design, construction and equipping of the International Specialized Hospital of Uganda at Lubowa. Another case to note is the Uneme Contract where Government of Uganda committed to compensate the company for any losses incurred during the negotiation of the contract. In Tanzania for example, a PPP financed projects between TANESCO, a government parastatal and two private entities i.e. independent Power Tanzania Ltd and Songas have led to TANESCO

covering losses made by the firms, currently worth 200 million USD.

Debt could also arise from direct liabilities and indirect-contingent liabilities. These could include financial obligations whose timing and magnitude depends on the occurrence of some uncertain future events outside the control of the partnering government. Events such as this could include a fall in the exchange rate of the host state's currency, or if the demand for the requested service or facility falls below a specified level, or during economic crises which could result into a reduction in the demand for a certain service or product being supplied by the PPP project. In view of these varying cases, many governments have been lured into compensating the private entities.

Public Authorities still bear the ultimate risk of project failure

Proponents of PPPs argue that it is possible to transfer project risks from the public to the private sector, experiences in the East Africa Community have revealed that it is in fact the public sector that bears the ultimate risk of project failure. In fact, risk transfer in PPPs is very limited. Given that public services need to continue uninterrupted, governments find it difficult to reject additional requests by the private partner or charging penalties for poor performance, because the entire PPP project may fail – so the private partner has a strong bargaining position.

In conclusion, the failure of PPPs to achieve their intended objectives in Europe should serve as lesson to the EAC partner states to consider reviewing their PPP approaches and legal frameworks to mitigate the inherent risks and maximize the benefits therein. Our experience shows that while PPPs provide an avenue through which developing states like the EAC partner states, can individually but also as a regional bloc, realize large investment projects, the nature and process of designing a number of PPP contracts should be undertaken consciously to ensure that they do not undermine inclusive development. Strong public financial management is fundamental because poor financial management of PPPs can have wide reaching economic impacts.

With PPPs being heralded as the next big thing for EAC's financing for development, this calls an urgent need to design clear and appropriate legal and financing frameworks for PPPs that promote appropriate risk sharing between the private party and the respective Governments. Moreover, this is in line with the new thinking that presents an alternative i.e. People First PPPs, as already embraced by the EU. "A People First PPP is a long term contractual relationship between the public and private sector, where delivering value for people is the core objective, there is a commitment to serving and protecting the community, and the project is developed with the real interests of people in mind."

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