U.S. Agency for International Development
International Finance Corporation

BIDFacility

Balkans Infrastructure Development Facility

Concept Paper

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www.bidfacility.com

LIST OF ABBREVIATIONS AND ACRONYMS

BIDFacility	Balkans Infrastructure Development Facility
DFIO	Department for International Development
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
IFC	International Finance Corporation
LIS	legal indicator survey
MOU	memorandum of understanding
OECD	Organization for Economic Cooperation and Development
PDF	project development facilities
PPIAF	Public Private Infrastructure Advisory Facility
PPP	public-private partnership
PSF	private sector financing
PSP	private sector participation
RIP	Regional Infrastructure Program
SIA	sponsoring institution and agency
UN/ECE	United Nations Economic Commission for Europe
UNCITRAL	United Nations Commission on International Trade Law
USAID	U.S. Agency for International Development

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Supporting Documentation is available on www.bidfacility.com on the following:
International Project Development Facility Survey

Project Development Process

Review of Relevant PPP Experience

I. OVERVIEW

The U.S. Agency for International Development's (USAID) Regional Infrastructure Program (RIP) was developed as an important aspect of the U.S. Government's overall support for achieving the objectives of the Stability Pact for South East Europe. One key element of RIP is promoting and facilitating the flow of private sector participation (PSP) in this region, primarily in the water and transportation sectors. Based on a review of more than 60 public-private partnership (PPP) projects, an international survey of project development facilities (PDF), and discussions with financial institutions, the RIP team concluded that a significant limitation to PSP in this region's infrastructure development is the lack of "bankable" project packages, supported by strong feasibility analyses and design, which would appeal to private sector investors. Furthermore, this research indicated that PDFs can be quite successful in overcoming these kinds of constraints.

This concept paper summarizes USAID's initiative to create a PDF for the region, to be named the "Balkans Infrastructure Development Facility" (BIDFacility). After a series of meetings with officers from the International Finance Corporation (IFC) of the World Bank Group, IFC management has agreed in principle[1] to join USAID in creating BIDFacility. Our goal is to introduce the idea to, and invite the participation of, other international financial institutions, multilateral development banks, bilateral donors, and governmental organizations. We estimate the initial startup costs and capitalization of BIDFacility to be about $10 million, with operations starting in 2003.

A number of preliminary discussions indicate that, in principle, there is interest in supporting and moving forward with this project. Clearly, BIDFacility could contribute to generate a larger and more solid stream of prospective targets for lending operations and therefore should be attractive to institutions interested in financing public-private infrastructure projects in the region. Donors and development agencies are also interested, to a large extent, because of the multiplier effect this revolving facility would have on their funding.

From the perspective of potential participants, there are two other important considerations: (1) given that BIDFacility is in the inception stage, an opportunity still exists to take part in its definitive design; and (2) participants can contribute to the capitalization of the PDF and/or to cover its operating expenses via in-kind contributions (e.g., staff, office space).

This concept paper describes concisely the rationale, preliminary design concepts, and *modus operandi* guidelines for the proposed facility. Lastly, we outline the next steps that will be followed in our effort to make BIDFacility become a reality.

[1] To be confirmed by approval of IFC's Board of Directors.

II. BACKGROUND AND RATIONALE

Since 2001, USAID has been funding and overseeing the RIP in South East Europe, which has helped promote and/or facilitate water and transportation infrastructure projects in the region through more than 40 different activities (visit www.see-rip.com for details). A key element of this program is facilitating the flow of private capital and management capacity to the region through PSP, including PPPs.

A key finding of one of RIP's recent assessment reports[2] was that a significant constraint to PSP in infrastructure development in the region was a lack of adequate feasibility analysis, project design, and financial structuring being performed by agencies sponsoring new infrastructure projects. International models of PDFs have demonstrated that such facilities can be successful in efforts to overcome these constraints. A comparative survey of international experiences with similar facilities was conducted and is available as a supporting document for reference. This survey covered 13 PDFs around the world and provided interesting insights for our purposes[3]. Appendix 1: A Survey of International Project Development Facility Experience summarizes the salient observations from this survey.

BIDFacility will be a project development mechanism to promote PSP in infrastructure in South East Europe. The proposed structure and capitalization of BIDFacility reflect the survey findings regarding ownership, structure, staffing, operations, and capitalization. All of the PDFs surveyed directly or indirectly support not only capacity building and services strengthening the enabling environment, but also project development technical assistance.

The main conclusions of the survey were as follows:

- There is precedent for the effective use of grants (rather than loans) to pay for project development assistance.
- Grant funds used for project development should be recovered from the transactions that close successfully.
- A minimum of $4million to $6million of PDF capitalization is required.
- Capacity building and enabling environment activities should be encouraged and supported, but the facility should focus on project development activities.
- The greatest need for PDF assistance is with small and medium-size projects.
- The survey also confirmed that a regional approach is feasible.
- BIDFacility's role will be to increase PSP in new infrastructure projects as a means of reducing the focus on public budgetary resources and increasing the quantity and quality of service delivery through private sector participation in infrastructure development. Within this framework, BIDFacility will use local professionals and outside consultants to build capacity not only in the sponsoring institutions and agencies (SIA), which serve as sponsors and

[2] Assessment Report of PPP in Infrastructure (USAID Regional Infrastructure Program (RIP).
[3] Infrastructure Project Development Facilities: A Survey of International Project Development Facility Experience—USAID (RIP).

future public sector partners of the private sector operators, but also in the local consulting market.

This concept envisions a PDF that would provide funding and technical assistance for project preparation and transaction structuring, on a cost-reimbursement basis (i.e., funds expended by the PDF in screening and appraising these investment opportunities would be reimbursed by building these costs into the financing of the PSP projects). The rationale behind offering such technical assistance is that SIAs often lack internal capacity in areas such as financial analysis and project design. These are necessary for developing PSP projects.

Other important contributions of PDFs are to help address weaknesses in the enabling environment through successful project development and to encourage good governance by making continued support of SIAs contingent on adherence to standards of international best practices in procurement, contracting, structuring, and negotiation (see Section IV.3, Enabling Environment).

III. VALUE TO THE DONOR COMMUNITY

USAID and IFC are inviting participation from international financial institutions, governments, and other donor community members to join in completing the design, capitalizing, and operating of the new BIDFacility for South East Europe. Key questions for this donor commitment likely include the following:

- *Why have a PDF?* A PDF is needed to develop bankable projects and attract private sector participation by subjecting public sector project proposals to private-sector standards of analysis, structure, and strategic planning. A PDF also will help improve the enabling environment and encourage better governance.
- *Who will benefit from the PDF?* Donors will see the impact of their funds significantly increased by financing multiple projects through the revolving fund structure. Private sector investors and management companies will gain access to better prepared projects with lower transaction costs. SIAs will gain access to a facility that helps them make their projects more attractive to the private sector. Ultimately, communities and citizens in the region will benefit from the improved infrastructure brought about by the activities of BIDFacility.
- *What form will the PDF take?* BIDFacility will be a small unit staffed by local and international professionals located in one or more offices in or near the Balkans region.
- *What will the PDF do?* The PDF will identify, analyze, structure, and package new infrastructure development projects for private sector investors' ownership, operation, and financing. BIDFacility will also serve to build capacity in public agencies and local consulting firms, thereby expanding the capacity of other stakeholders to increase PSP in service delivery.
- *Who will be the PDF's clients?* BIDFacility will assist SIAs, private project developers, donors, and International Financial Institutions (IFI) in moving projects toward financial closure. As such, the facility will be designed to interact with all of these stakeholders.

USAID is funding the design costs for BIDFacility, including a comprehensive business plan and Investment Memorandum, with direct involvement by IFC staff. Furthermore, USAID and IFC have agreed in principle to join other donor, governmental, multilateral, or private organizations in financing and operating the new facility. The benefits to organizations that participate in the financing of this project are as follows:

- Increased availability of infrastructure projects attractive for lending activities
- Improved infrastructure service delivery and resulting political support
- Improved corporate governance in the region
- Improved enabling environment
- Leadership position in cutting edge PSP methodologies

A multiplier effect on the potential impact of the financial resources used.

In addition to the concurrence of IFC to participate in developing BIDFacility, initial discussions with other prospective participants have been encouraging. During 2002, meetings were held with EBRD, EIB, EU-CARD, and EU-PHARE, during which it was generally agreed that BIDFacility was an important initiative that should be pursued. Discussions of BIDFacility were held at the Stability Pact Working Table II meetings in Sofia in June 2002. More recently, meetings were held with EIB's Special Coordinator for the Balkans and the Stability Pact Investment Compact, and the Director of the Stability Pact Working Table II. These meetings generated additional interest in the BIDFacility proposal. The U.S. State Department's Coordinator for the Stability Pact has also indicated that BIDFacility is a needed and valuable concept. The structure and purpose of BIDFacility is consistent with the PDF type organizations that the IFC promoted and presently manages, such as the Africa Project Development Facility and the Mekong Project Development Facility.

IV. DESIGN CONSIDERATIONS

From the point of view of how to structure the new PDF, there are different dimensions to consider. First, given the above stated objectives, we need to look at options for capitalizing BIDFacility and covering its operating costs. These are clearly related to the scope of activities that the PDF intends to cover i.e., how far in the "continuum" of the project development process it will go. A third important consideration is the need to address institutional and legal weaknesses that affect PSP in infrastructure projects in this region, in order to achieve an appropriate enabling environment for this purpose. Then, there are different options for sector emphasis, as well as for geographic focus that will have an impact on the operating model and thus, need to be taken into account. Although these different variables are interrelated in practice, we will look at them separately.

IV.1 Capitalization and Operating Approaches

Most PDFs are structured to provide cost recovery only on deals that reach financial closure. Therefore, funds spent on deals that do not close are lost and the PDF eventually runs out of money, staying in operation only long enough to achieve the service delivery and capacity-building objectives referred to above.

An alternative structure for PDFs is to seek reimbursement for more than its actual costs for each deal to make up for the shortfall resulting from deals that never close. With this structure the PDF would continue to exist in perpetuity. The attractiveness of a full cost recovery structure is that the PDF could eventually be turned over to a private sector operator. This privatized entity could then become a facilitator and/or source of infrastructure project finance, becoming an important catalyst for future private sector participation in financing and operating new infrastructure development projects.

However, having performed some financial simulations, our PDF design team has concluded that the full cost recovery model would be too costly to be feasible at present. Nevertheless, this model remains as an option for future consideration of the entities that join us in the capitalization and operation of BIDFacility.

There are two categories of PDF funding requirements: (1) capital that will be used to pay consultants and financial advisors to conduct project development activities for SIAs; and (2) capital that will be used to cover the PDF's operating expenses. Although category (1) funding will come directly from the capital pledged by the participating PDF members several options exist for covering category (2) expenses. These options include a) using contributions from international organizations or donors, b) using contributions from host countries in the region, and/or c) building these costs into each transaction. Contributions could be in the form of PDF staff being paid by a donor or government entity, and/or providing in-kind assistance (e.g., office space, communications equipment, and administrative support.)

From an operational viewpoint, PDFs can either pay the consultants hired to provide technical assistance to SIAs directly, or they can loan the required funds to SIAs, who will then pay the consultants. The PDF design team recommends that the PDF pay the consultants directly, given concerns about capacity, transparency, and other important factors associated with SIAs handling procurement funds. Direct payment by the PDF is also likely to be more efficient and expedient than going through SIAs.

The current trend in PDFs is that the financing of projects reimburses the facility for funds expended on project preparation and feasibility studies. As mentioned earlier, not all deals will eventually reach financial closure; in those cases, there will be no financing package to provide such cost reimbursement. If the failure to reach closure is the result of SIAs not having performed its duties under the terms of its memorandum of understanding (MOU) with the PDF, then SIAs must reimburse these costs. If the failure is not the result of SIA lack of performance, then the PDF absorbs the loss, leading to a gradual decline in capital balances over several years.

The PDF design team has also prepared a financial model (spreadsheet) for a 10-year PDF, which is provided as **Attachment 2** to this concept paper. The model illustrates the financial implications of values estimated or chosen for a number of variables affecting the functioning of BIDFacility. One element of this spreadsheet permits the user to examine the stages of transaction closure following the feasibility study to evaluate the impact of different scenarios and cost estimates for on BIDFacility's longevity and performance.

The numbers presented in the BIDFacility financial model take into account the survey findings regarding deal flow, deal size mix, percentage of deals reaching close of financing, average cost of providing technical assistance for each deal, and cost recovery collection rates.

IV.2 Role of the PDF in the Project Development Process

It is important to examine how far BIDFacility should go in the project development "continuum," beyond providing technical assistance for the completion of a comprehensive feasibility study that meets the requirements of private sector sources of project financing. The feasibility study itself will have at least three different components: (1) engineering and technical analysis, (2) economic and financial viability analysis, and (3) organizational and operational requirements. However, there are other stages in the project development process in which advisory services will be needed, including the drafting of tender and bidding documents and contracts, prequalification of suitable prospective investors, assistance in evaluating bids, selection of and negotiations with winning bidders, and post-award monitoring and evaluation.

An important element to the project development process is the way in which negotiations among SIAs and investors structure the transaction to address weaknesses in the enabling environment, such as tariff or rate structures. The PDF design team has looked separately into the steps typically involved in this continuum or project development process. The team has made an initial attempt to estimate the costs involved in each of these stages, giving careful consideration to which of the interested parties should cover these costs.

As shown in a second supporting document prepared by our design team,[4] it is not easy to estimate the average costs associated with these transaction costs because of the differences

[4] "Project Development Process and Related Costs Analysis."

in size and complexity between projects and sectors and between PPPs and private sector financing (PSF) projects. The project development process can be broken down into individual steps, each with its own associated costs and set of players. The initial development steps, or pretransaction phase, are as follows:

- Identify project
- Analyze debt capacity
- Determine capacity enhancement initiatives
- Conduct prefeasibility studies
- Conduct feasibility studies, including review of alternative financing structures.

Once the steps above are successfully completed, the project enters the transaction phase, which includes the following steps:

- Provide financial structuring and prepare tendering documents
- Prequalify bidders and/or bidders' conference(s)
- Evaluate offers and select contractor(s)
- Negotiate the final agreement
- Undertake due diligence and assist in closing all financial agreements.

To facilitate the financing of smaller scale projects that typically fall below the financing threshold of IFI and commercial lending institutions, BIDFacility will bundle smaller projects for pooled financing to attain the critical mass necessary to attract private sector investors.

The PDF design team recommends that BIDFacility engage in the project development process, being careful not to expend resources on traditional capacity-building efforts typically financed by donor agencies and IFIs' technical assistance funding. Although it is anticipated that the deal flow will be generated by SIAs, private sector developers, and IFIs, BIDFacility will not consider projects any earlier than the prefeasibility study, unless specifically requested by the IFIs. Finally, to preserve resources, BIDFacility will avoid very large high-cost, long-term development projects.

The business plan will also assume that once BIDFacility is engaged, it will remain involved with the project through financial closure. This is designed to ensure that SIAs are assisted throughout the latter stages of project development and ensure that the final outcome is positive for SIAs and BIDFacility.

IV.3 The Enabling Environment

In most of the Balkans nations, there are weaknesses in many of the laws and regulations governing tariffs, concessions, municipal borrowing authority, and other issues affecting infrastructure, especially infrastructure operated and/or constructed with PSP. Many domestic and donor organizations are working to improve the enabling environment; however, these weaknesses still constitute a significant barrier to PPP and PSP, raising the costs of bringing transactions to closure.

At the international level, there are numerous donor programs that address weaknesses of the enabling environment. The United Nations Economic Commission for Europe (UN/ECE) has made a valuable contribution in addressing the enabling environment, particularly the recent creation of a Regional Flagship Initiative and a Public Private Partnership Alliance. Another UN body, the Commission on International Trade Law (UNCITRAL), has prepared a Legislative Guide on Privately Financed Infrastructure Projects. This guide has become the starting point for governments preparing new laws or reviewing the adequacy of existing concession law. Similarly, the Organization for Economic Cooperation and Development (OECD) has developed a model concession law, which will be used as a benchmark in the region. EBRD's annual Legal Indicator Survey (LIS) also makes a substantial contribution in assessing the legal framework for concessions in transition countries.

On a broader front, the World Bank-implemented Public Private Infrastructure Advisory Facility (PPIAF), which combines donor contributions to support analysis and development of the enabling environment worldwide, has conducted programs in South East Europe as part of its mandate. The European Union has a number of initiatives that strengthen the enabling environment for PPPs. Other bilateral donor efforts, such as USAID's local government initiatives, have begun the process of broad financial reform and institutional strengthening in various municipalities. Efforts by various donors to assist in building the legal underpinnings, which are spurring the evolution of capital markets in the region, have also strengthened the enabling environment for PSP.

Although these programs focus on developing and harmonizing the general framework for private sector investments, preparing guidelines on best practices, developing negotiation platforms, and creating educational programs for local officials, BIDFacility will focus specifically on individual projects. Given that concession contracting is a once-in-a-decade experience for most local governments, most SIAs do not retain in-house expertise in this area. Although training programs and best practices manuals are helpful in raising awareness of the benefits of PPP initiatives, BIDFacility will augment these initiatives with specific transaction-based assistance to local governments as they partner with the private sector.

The BIDFacility design team envisions a process of tailoring each transaction to address weaknesses in the enabling environment. Although this tailoring process is typically focused on the negotiation phase of transactions, raising costs for the private sector participant, the team sees this tailoring occurring at earlier stages of project development within BIDFacility. Specifically, these stages include the distribution of background materials to potential applicants, an extensive application for BIDFacility assistance, a model version of the MOU signed between BIDFacility and SIAs, a model contract, and the actual signing of the MOU. At each of these points, weaknesses in the enabling environment will be illuminated and, as each of the stages progresses, BIDFacility will work with SIAs to identify ways in which the transaction can be tailored to address these weaknesses.

BIDFacility will also assist SIAs in bringing fairness and transparency to their project development, to the related bidding and procurement processes, and to the eventual operation of the projects. One difficulty PSP projects have encountered in the development and operation phases relates to the way in which the public perceives the SIA has dealt with the fairness and transparency of the process, the environmental accountability of the project, and social mitigation measures implemented as part of the program. Public concerns can relate to tariff increases, elimination of labor redundancy, environmental impacts, corrupt contracting, and other issues. BIDFacility will work with SIAs to address these issues, to make the project development process as open and accountable as possible, helping SIAs understand how to make the measures taken to address these concerns clear to the public.

The BIDFacility team also recognizes that there is no optimum enabling environment for PPP initiatives. As such, it is difficult to draft legal and regulatory frameworks for PPPs in the abstract. PPP initiatives can therefore be beneficial in helping to formulate and accelerate the development of framework initiatives.

Experience in the region reveals that developing a comprehensive framework in concert with a specific project can be extremely valuable to the local SIA and to national policy makers. The BIDFacility team therefore does not view national enabling initiatives and specific project initiatives as mutually exclusive; rather, it views them as complementary. For example, the Slovenian government's efforts to develop concession projects were successful in several instances in the absence of a single framework law but led to the joint effort by the Slovenian government and EBRD to develop specific concession framework legislation. Similarly, the Tallinn, Estonia, water privatization project approved in 2001, is driving the creation of a municipal tariff setting regulator by 2005.

Finally, the BIDFacility team recognizes that PPP and PSP are both organic processes that are constantly evolving based on global capital market conditions, host country macroeconomic factors, changes in corporate culture, and an evolving public perception of the costs and benefits of these partnerships. The validity of a national framework therefore can be tested only by the advancement of specific projects.

In conclusion, the PDF design team recommends that BIDFacility stay focused on developing and promoting the execution of specific projects, while other vehicles and entities take responsibility for technical assistance and institutional strengthening.

IV.4 Sectoral Focus

In designing a new PDF, decisions must also be made regarding the targeted sectors. Naturally, there are advantages and disadvantages associated with the decisions made. The RIP focuses on water and transport; therefore, there is interest in bringing these sectors into the BIDFacility's mandate.

However, some would argue that for BIDFacility to be in the greatest demand, its mandate should cover all categories of infrastructure projects, including energy, construction, and health. A multisector PDF can benefit from an ability to select its projects from a wider range of options, and in doing so it can better manage its risk through the diversification of its portfolio. Different sectors also tend to have different cycles, so the PDF could move into sectors when they are doing well and out of them when not. The downside of a broad multisector strategy is that it is likely to be more complicated to manage than one that focuses on only a handful of sectors. From a staffing viewpoint, a multisector strategy would also require the PDF to have a pool of expatriate sector specialists from which it could draw on an as-needed basis.

Undoubtedly, the organizations that will participate in capitalizing BIDFacility and/or contributing to its operating costs may have sector-specific goals and policies that should be furthered by the BIDFacility's operations. For example, initial consultations with certain stakeholders have indicated that housing might be an appropriate sector for BIDFacility activity. The host country governments are also likely to have priorities that must be addressed by the PDF, and certainly one of the tests of any application submitted to the PDF for assistance will be the government's priority within that sector.

In a paper commissioned by Britain's Department for International Development (DFID) to examine the viability and possible *modus operandi* of private sector investment promotion mechanisms in developing countries, the authors conclude that "there are situations where lack of preinvestment to create business opportunities is the binding constraint on private investment," but caution that this is not true across sectors. For example, the authors note that in industries like oil and hard rock mining, private preinvestment commitments will be made anyway because companies will have no alternative but to go where the resources are located. In principle, the sectors in which they see these promotion mechanisms having a higher justification and playing a more important role are the infrastructure ones—most obviously, power, water, gas distribution, and roads infrastructure.[5]

In conclusion, although the specific sectors remain to be defined as part of the business plan through a market survey and SIAs', donors', and IFIs' preferences, one attractive option is to get started by concentrating on only a few key sectors (e.g., water, transport, and energy). This effort would leave open the possibility of assisting in other infrastructure projects as a second tier and gradually adding additional sectors, if appropriate, as opportunities arise during PDF operations. Therefore, with this sectoral focus, BIDFacility might support such projects as a concession for water and wastewater facilities in a Balkans city (e.g., Bucharest), a subsovereign loan from a private bank to upgrade the lighting system in a city (e.g., Sofia), or an agreement with a national port authority to upgrade and operate port facilities (e.g., Rijeka, Croatia).

IV.5 Multicountry Territory

Another aspect to be decided by those who will be capitalizing BIDFacility is: If not all, in which countries will BIDFacility conduct its activities? Factors to consider are: How much money will the host countries be able to contribute to the operating expenses of the PDF? What is the potential for PSP in infrastructure development in each country? What is the capacity of the economy to generate and absorb PSP deal flows?

[5] "Justification and Possible Modus Operandi for Public Sector/Donor Support for Generation of Business Opportunities in Developing Countries," Cambridge Economic Policy Associates for DFID

The PDF design team recommends a multicountry territory, where the participation of all Balkans countries is determined by demand. These nations include Albania, Bosnia/Herzegovina, Bulgaria, Croatia, Macedonia, Serbia/Montenegro, and Romania. Countries like Serbia or Romania might have a higher level of demand for PDF assistance because of their size, but BIDFacility will endeavor to be active wherever demand exists. Some stakeholders have suggested that BIDFacility should have country teams that mobilize activity via in-country satellite offices, drawing support from BIDFacility headquarters, which may or may not be located within the Balkans. (In any event, stakeholders emphasize that any expatriate advisors should be long term so that they can learn the regional business practices and “rules of the game.”) If the PDF is linked to a given country’s national budget resources or to a financial institution that operates in only one country, then it would be restricted to operating in only that country. If the PDF is linked to donor budget resources, and those donors agree on which countries will receive PDF support, or is linked to a financial institution that conducts business in multiple countries, then the PDF can operate in multiple countries. For this review, “linked” means that the PDF is housed in the offices of that organization, possibly having a representative in the local offices in multiple countries, and that organization is a potential source of capital for PSP project finance.

Another important factor to consider relates to potential problems in dealing with inconsistent or even contradictory laws among the various countries. It will be necessary to understand the comparative legal framework in the territory, and the PDF will need to obtain the required legal status and licenses or permits to conduct business in those jurisdictions where it plans to operate.

As in the other design considerations discussed above, a detailed market analysis, which will be performed as part of the business plan, will be the determining factor in deciding in which countries BIDFacility will become active in first, with the understanding that it will go from there to satisfying the demand for viable PSP interventions in the other countries, as it develops.

V. INSTITUTIONAL AND OPERATIONAL ASPECTS

To ensure maximum utilization of the PDF by SIAs, PDFs are often located in, or are at least directly related to, a potential source of project finance. In single country models, the PDFs are often housed in a Ministry of Finance or national development bank that has influence over budget allocations and access to other financial resources, or in financial institutions that have an interest in financing projects within the host country. For BIDFacility, however, a multicountry model is envisioned. In that model, a PDF could be housed in the local representation office of a donor organization or of a regional or international financial institution.

Cost reimbursement to the PDF should be built into each transaction, and potentially private companies could be willing to engage BIDFacility on a retainer basis as an advisor for infrastructure, which could be another source of steady cash flow. The percentage of total costs for such transactions will have to be determined through the preparation of a business plan in which the costs of consultants, and the breakdown of these costs by size of project, are all calculated. This plan will provide the level of SIA participation that BIDFacility would need to require to stay in operation for a targeted time period, such as 5 or 10 years. The exact tenure of BIDFacility and the number of deals it can support within its proposed capitalization are greatly dependent on a number of assumptions addressing the success rate, how far through the project development process “continuum” BIDFacility provides support, and other factors. Initial variables addressing these assumptions are provided in the spreadsheet model provided in **Attachment 2** of this concept paper. Some scenarios show BIDFacility lasting well beyond 10 years, whereas others show it declining within 5 years, depending on the assumptions used and the level of capitalization. The default values in the spreadsheet are for a 10-year facility.

The PPPs and PSF are assumed to include investments by both the private sector participant and the public sector (SIA) partner. Therefore, SIA participation in compensating the PDF for the costs of its support is considered essential because (1) a tangible “buy-in” demonstrates real SIA commitment to the transaction, (2) the PDF will not be financially sustainable unless there is involvement from SIAs, and (3) it would not be reasonable to expect the private sector to take on all of the risks associated with the first phase (feasibility analysis) of technical assistance.

Limiting PDF costs will be important in keeping its services attractive to SIAs and private sector investors. To control costs, the PDF could attempt to negotiate reduced rates from the consultants that will be hired. This effort can be achieved by sending periodic invitations to prospective consultants to submit credentials so as to include on the BIDFacility list of prequalified consultants. International experience indicates that consultants are often willing to discount their rates in order to get on the prequalified list, which serves much the same role as an Indefinite Quantity Contract (IQC). These efforts will have to be undertaken carefully to avoid an adverse effect on the quality of consulting services and to the extent that it has meaningful impact.

Cost control can also be exercised in the completion of feasibility studies by ensuring that the more advanced phases of the work take place only when the initial stages indicate that the project is likely to be viable. Furthermore, the PDF could partially compensate consultants and financial or legal advisors for the completion of project development tasks via success fees built into the financial arrangements of the transactions, taking due care to avoid any potential conflict of interest.

When clients apply to BIDFacility for assistance, the process will begin with a prequalification application procedure in which the basics of the proposed project are presented in sufficient detail to enable BIDFacility to ascertain whether the project has a reasonable probability of success. This application will therefore include not only a technical description of the project but also a credit worthiness analysis of the relevant SIA. The clients may have to incur some small consulting expenses in the preparation of these applications. BIDFacility can provide clients with a list of prequalified consultants who have demonstrated expertise in the preparation of such applications but will not endorse a specific consultant. The essence of the application is a description of the proposed project, along with a basic financial profile. The PDF will analyze the project but will not hire consultants to conduct the feasibility study unless the project appears to meet at least certain minimal criteria.

VI. NEAR-TERM OUTLOOK

This concept paper has covered the background, rationale, preliminary design elements, and operational guidelines for an infrastructure PDF in the Balkans region. Initial discussions with prospective participants continue to take place, and feedback from earlier meetings is being received.

There are several components to the BIDFacility financing package:

- Design costs estimated at $400,000 (USAID)
- Initial startup and capitalization costs estimated at $10 million (USAID, IFC, bilateral donors, IFIs)
- Local currency contributions to operating expenses (SIAs, host countries)
- In-kind contributions to cover some operating costs (all)
- Long-term expatriate consultant(s) (donors, IFIs)
- Multiple short-term expatriate consultants (donors, IFIs)
- Retainer contracts with private companies interested in the Balkans.

As stated earlier, USAID is funding the initial design costs, which include preparing a detailed business plan and investment memorandum, and has made the first pledge for the capitalization of BIDFacility ($1.5 million). IFC has joined in the design effort and has indicated a willingness to invest between $1 million and $2 million (subject to Board approval) in the capitalization of PDF. Financial participation from other donors and financial institutions is sought to cover other costs as outlined above. International models of PDFs often include funding from multiple donors; i.e., the model recommended by the PDF design team. Furthermore, given the regional mandate of BIDFacility, it would be appropriate to have multiple donor participation. Ideally, donor contributions will be untied so as to enable internationally competitive bidding processes.

Members of the IFIs and donor community who are potentially interested in participating, after reviewing this document, will have discussions with USAID and IFC regarding the form and substance of such participation.

The BIDFacility design team is prepared to visit the donor and IFI community before the end of the year to discuss their willingness to support BIDFacility. Once it is clear that sufficient capitalization pledges have been made, a detailed business plan and investment memorandum will be prepared. Subsequently, the founding members of BIDFacility will organize a donors' conference to confirm the commitments made. The rollout and startup of operations is envisioned to take place in 2003.

CONTACT INFORMATION

Carl Mitchell
Europe and Eurasia Bureau
U.S. Agency for International Development
Tel. (202) 712-5495
Fax: (202) 974-4318
cmitchell@usaid.gov

Giuliano Caloia
Infrastructure Department
International Finance Corporation
Tel: (202) 473-0133
Fax (202) 216-3014
gcaloia@ifc.org

www.bidfacility.com

APPENDIX 1: Project Development Facilities: A Survey of International Experience

Survey Summary

Facility	Established Capital	Mandate	Sectors	Management/ Operating Budget	Governance	Level of Activity/ Average Intervention	Cost Recovery
Philippines LGU PIPDF (single country)	2000 $5.5 million Govt 915K	Project Preparation Transaction Support	Roads, bridges, ports, water supply and sanitation, solid waste disposal, and others on a case-by-case basis	Management by staff of Philippines Land Bank. Operating budget: ADB $3 million loan with $600,000 grant & $915,000 Govt grant	Board of Directors	10 projects to be funded Average cost: $300,000	Total; TA is funded by loans to LGUs
South Africa MIIU PDF (single country)	1989 $12.17 million	Project Preparation Transaction Support	Very active in the water sector. Closed a large solid waste project for Johannesburg.	CEO, 8 staff $1.43 million	Board of Directors	23 projects completed Average cost: $206,500	Partial; recent change from grant system to grant, loan, and fee TA.
South Africa P3 Unit PDF (single country)	2002 $6 million	Project Preparation Deal flow for PPP Unit	Only for national and provincial level projects (no water deals). A focus on PPP in health care, facilities management, IT, and transport systems.	Head of P3 Unit, 4 local staff 1 donor funded resident expat advisor is planned	PDF is not a separate legal entity. Contract is between the SIAs and the PPP Unit and capitalization is kept in a Treasury account	5 projects projected to be completed in year 1 Average cost: $225,000	Total for deals that close, but costs for non closures will be $6 million over 10 years
Africa PDF (regional)	1986 $22 million	SME Development Business Advisory (BAS) Enterprise Support (ESS)	15% Agriculture 10% Agribusiness 35% Manufacturing 10% Tourism 30% Services	CEO, 57 staff About $3 million per year	Board of Directors	45 BAS interventions 88 ESS interventions Average cost: $7,633 (1.29% of project finance)	Partial: $790,452 out of $1,015,152
Africa Management Services Company (regional) (28% private ownership)	1989 $55 million	SME Development Capacity Building	35% Manufacturing 30% Banking 20% Services 15% Agriculture	CEO, 53 staff: 25 in Amsterdam 32 in Africa About $3.7 million per year	Board of Directors	124 interventions as follows: 55 small (client <$5 million) 37 medium ($5-10 million) 32 large (>$10 million) Average cost: $160,484	Partial: 94%
Mekong PDF (regional)	1997 $25 million	SME Development Project Preparation Capacity Building	28% Manufacturing 21% Textiles 18% Paper & wood 9% Tourism 9% Agribusiness 6% Plastics 3% Fisheries 3% Education 3% Transportation	Manager, 48 staff $4.2 million per year	Advisory Board Board of Donors	38 projects completed Average cost: $590,000	Partial; total of $174,133 collected in last year

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Indonesia PSPDF (single country)	Design phase $5 million	Project Preparation Transaction Support Capacity Building	Water Electricity Transport	TBD – still in design phase	Other	TBD – still in design phase	TBD – still in design phase
Egypt PSPDF (single country)	Design phase $7.5 million	Project Preparation Transaction Support	Water only	Local General Manager, resident expat finance and civil engineering technical advisors, 2 local admin.	Board of Trustees	TBD – still in design phase	TBD – still in design phase. Plans on 1/3 cost recovery
China PDF (single country)	2002 $17 million	SME Development Capacity Building	TBD – new facility	TBD – new facility	Board of Directors	TBD – new facility	TBD - partial planned
Southeast Europe Enterprise Development (regional)	2000 $33 million	SME Development Enterprise-Level Investment Services Capacity Building	5% Education 25% Construction 5% Banking 40% Agribusiness 20% Manufacturing 5% Tourism	General Manager, 53 full-time staff	Board of Donors	6 projects completed FY01 Average cost: $400,000	Partial
South Pacific PDF (regional)	1990 $10.5 million	SME Development Capacity Building	30% Manufacturing 10% Tourism 10% Agribusiness 25% Fisheries 25% Services	Regional Manager, 10 staff $2.42 million	Advisory Board	30 projects completed FY01 Total financings: $9,920,000 Average financing: $450,000 Average cost: $110,000	Partial; fees invoiced were $57,486 total
Bangladesh PSIDF (single country)	1997 $21 million	Project Preparation Transaction Support Capacity Building	Strong emphasis on the energy sector, mandate includes telecom, transport, water	World Bank Task Manager, resident General Manager and support staff. Operates through IDCOL, a private company organized by the GOP.	IFC and donors, with consultation from Citibank advisors. Operating budget submitted every May to WB for approval.	Very little progress other than $30 million IFC investment, with other donors and private sector financiers, for Lasmo Oil Pakistan to produce gas from the Bhit field.	No
Sri Lanka PSIDF (single country)	1995 $7 million	Project Preparation Transaction Support	Telecom, energy, water, transport	General Manager, 8 staff $835,000 per year overhead $3.5 million per year TA Operates through PSICD, a private company organized by the Government of Sri Lanka	IFC and donors, with consultation from Citibank advisors. Operating budget submitted annually to WB for approval.	Goal is 13 projects/year $160MM total project finance $12MM finance per project (40% of total project finance) $270K TA per project TA=2.25% of project finance	No