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PPIAF'S WORK IN EASTERN EUROPE AND CENTRAL ASIA

The global financial crisis that began in late 2008 set back ambitious infrastructure development plans among many countries in the Eastern Europe and Central Asia (ECA) Region. Many such plans relied on public-private partnership (PPP) arrangements. The flight to quality projects and countries perceived as less risky has been notable. Across the region, each project structure exhibited unique risks, but since the crisis, increased complexity and longer times between contract signature and financial close have been common.

Since inception PPIAF and its Sub-National Technical Assistance (SNTA) program have provided \$24,069,430 in funding to 105 projects in the Eastern Europe and Central Asia region, representing 12% of PPIAF's total portfolio. Armenia dominates the regional portfolio, with 13 projects worth \$3.5 million approved since inception. Croatia, with six activities, has the next highest number of activities, followed closely by Bosnia and Herzegovina, Bulgaria, Macedonia, and Turkey with five activities each. Energy and multi-sector activities represent 34% and 20% respectively of PPIAF's portfolio in the region.

In recent months, PPIAF approved one activity in Armenia to develop a financing plan for the Loriberd Hydropower Project; one activity in Turkmenistan to develop the Port of Turkmenbashi through private sector involvement; one activity in Azerbaijan to develop a national strategy for integrated solid waste management; one regional workshop to address the challenges of doing PPPs in specific sectors in the Black Sea Region, the Caucasus, and Central Asia; and one activity in Moldova to improve energy supply in the capital city, Chisinau.

The Eastern Europe and Central Asia region has seen investment in infrastructure projects with private participation grow by 80%, emerging as a leader among other developing regions. However, the financial crisis has had an adverse impact on private sector funding flows: investment levels have since dropped significantly lower than in previous years, and at a much higher rate than that other developing regions.

Nevertheless, in 2010 the city of saint Petersburg reached financial close for a 30-year concession contract for the rehabilitation, expansion, and management of saint Petersburg's Pulkovo International Airport. This was one of the first concession projects in Russia reaching financial close in the context of the global financial crisis. Despite this success, the PPP project pipeline in Russia was far more ambitious and included other multi-billion projects. This example shows that the crisis has led private investors to become more discriminating, a development similar to what was observed in the bond market.

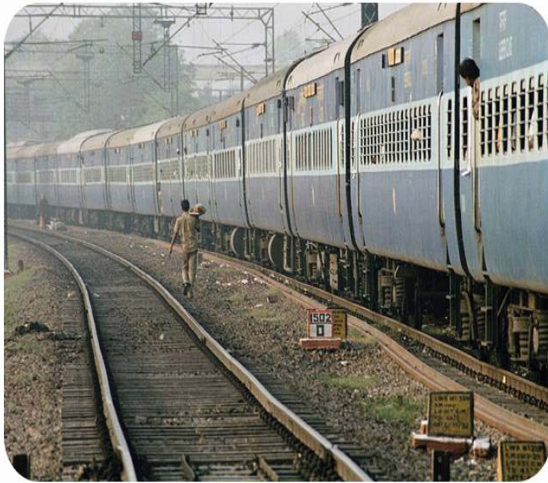
PPIAF support to Eastern Europe and Central Asia has continued to focus on the Balkan states and various regional initiatives. The region's many small, landlocked countries look to regional cooperation as a key to solving major challenges in infrastructure. Several PPIAF grants have been aimed at supporting such cooperation. For example, PPIAF support to the Caspian Development Corporation is aimed at helping to create a new gas transmission corridor from the Caspian Sea to Eastern Europe. Along similar lines, PPIAF is also supporting the development of a wholesale electricity market in Southeastern Europe in order to achieve greater economies of scale. Follow-up support for the Central Asia–South Asia Regional Electricity Market will help Central Asian countries generate revenue by selling surplus electricity to Afghanistan and Pakistan.

On December 13–18, 2010, a workshop took place in Istanbul on the challenges of doing PPPs in the Black Sea Region, the Caucasus, and Central Asia. The workshop was organized by the United Nations Economic Commission for Europe (UNECE) with financial support from PPIAF, in collaboration with the Black Sea Economic Cooperation and the International PPP Platform Turkey. Fifty-one delegates from countries in the region such as Belarus, Bosnia and Herzegovina, Kyrgyzstan, Poland, Turkey, and Ukraine participated in the workshop. The majority of the participants came from PPP Units at the central level in their countries, but there were also representatives from independent think-tanks interested in PPPs, as well as representatives from the Turkish Treasury.

The main target audience of this workshop consisted of countries in Central Asia, where the need to develop modern transport and energy infrastructure, efficient border crossings, and effective municipal and social services is particularly acute, but where there is also very limited domestic expertise for preparing, assessing, and launching a PPP program. Despite this specific focus, it soon became evident that the issues discussed were equally relevant to the other countries represented in the seminar. With the exception of Poland and Turkey, these other countries are at the early stages of developing a PPP program. Some have already participated in one or a few transactions, while others have still to launch a PPP program (notwithstanding the occasional isolated transaction). Therefore, the organization of the workshop around key basic issues such as “what it takes to undertake effectively sustainable PPPs,” “risk allocation in PPP contracts,” “legal issues,” and “financial aspects” was appropriate.

Armenia: Strategy for Private Sector Participation in Armenian Railways

PPIAF Funding (four activities): \$966,200



Background: Since 2005, the government of Armenia (GOA) requested PPIAF assistance to restructure the country's railways with the objective of developing a restructuring plan to increase private sector participation in the rail sector. Transaction support was also required to structure the concession for Armenian Railway to attract a private investor and for the corresponding road show. At the time, the company was not productive, was expensive to operate and required government subsidies of more than \$360 million over the next 15 years, provided an expensive service to its customers and increasingly was less competitive; it needed lots of capital to improve its operations and provide a better service.

PPIAF's Contribution: PPIAF's extensive technical assistance in support of the country's railways and its concession covered the following areas:

- Strategy for private sector participation in Armenia Railway, analyzing the options to restructure it. The main recommendations of the PPIAF-funded study were: to reorganize the existing railway and begin implementing cost reductions, to implement cost accounting system changes to support all other efforts, to initiate a passenger services study to determine more cost effective methods to provide passenger transport services, to revise the draft railway law prepared by the GOA to permit the concessioning of the company to the private sector and to reduce regulatory burdens, to develop and implement human resources programs to mitigate the impacts from cost reductions and restructuring efforts, and to concession Armenia Railway under a full concession, as it was the modality that provided the greatest financial returns to both the GOA and the concessionaire. This study also contained a human resource plan, an analysis of freight markets, a forecast of traffic, and a plan to revise accounting to create an infrastructure cost center and passenger and freight profit centers.
- Preparation of the appropriate legal framework, concession design, and design of the regime necessary for the implementation and oversight of the concession.
- Support of the road show which was held in London in collaboration with the European Bank for Reconstruction and Development.

Outcomes: The government passed a decree to award a concession contract to a private operator and signed the railways concession contract on February 13, 2008. The 30-year concession agreement was signed between Russian Railway Company (RZD) and the GOA on February 13, 2008. South Caucasian Railways was incorporated by the winning bidder to run the railway and operate the concession. RZD paid an initial concession fee of \$5 million and agreed to pay annually, over 30 years, 2% of Armenia Railway revenue on freight transport services; it also agreed to invest about \$400 million in railway infrastructure over 30 years and an additional \$170 million to upgrade the rolling stock.

Post-conflict countries are another area of focus in the region. Countries emerging from a devastating conflict need to rapidly restore access to basic services for their population. While donors usually stand ready with generous reconstruction packages, the conflict may have left local institutions ill equipped to make good use of those resources. The traditional solution, involving technical assistance delivered by international consultants, has often proved disappointing. An alternative is to bring in a professional operator for a few years through a management contract. In Bosnia and Herzegovina, for example, PPIAF is helping the government examine options for private participation at the port of Brcko. In Serbia PPIAF is funding a study on electronic toll collection systems aimed at helping the government improve the efficiency of highway management.

PPIAF responded quickly and provided assistance in FY2009 to meet the emerging needs resulting from the financial crisis. In Croatia, PPIAF is assisting the government strengthen its legal and institutional framework and develop risk assessment models. In the former Yugoslav Republic of Macedonia, PPIAF support to the government is helping to improve the investment climate for private participation in the power sector. Furthermore, in Kazakhstan a PPIAF grant is helping to build the capacity of the central PPP unit to develop projects in the difficult crisis environment.

PPIAF ACTIVITIES APPROVED IN RECENT MONTHS

- **Armenia:** Development of Financing Mix and Financing Plan for the Loriberd Hydropower Project, approved on March 4, 2011, **\$150,000**
- **Turkmenistan:** Enhancing Private Sector Participation at the Port of Turkmenbashi, approved on January 19, 2011, **\$150,000**
- **Azerbaijan:** National Solid Waste Management Performance Improvement and Private Sector Participation Strategy, approved on December 6, 2010, **\$74, 950**
- **Europe and Central Asia:** Addressing the Challenge of doing PPPs in Specific Sectors in the Black Sea Region, the Caucasus and Central Asia, approved on November 16, 2010, **\$35,500**
- **Moldova:** Energy Supply Improvement Project in Chisinau, approved on October 1, 2010, **\$75,000**

PPIAF has activities in: Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Federal Republic of Serbia and Montenegro, Georgia, Hungary, Kazakhstan, Kosovo, Kyrgyz Republic, Latvia, Lithuania, Macedonia, Moldova, Montenegro, Romania, Russia, Serbia, Slovakia, Tajikistan, Turkey, Turkmenistan, Ukraine, and Uzbekistan