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IFC SmartLessons

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Delivering the Goods: Multi-Donor Approaches to Project Development and Funding

Getting a number of bilateral and multilateral donors to collaborate on the development and funding of partnerships with the private sector can be a daunting task. The IFC has, however, participated in such a partnership—the Private Infrastructure Development Group—which has successfully delivered results on the ground.

Background

In 2000 the UK government, through the Department for International Development (DFID), reached the conclusion that it made sense to use aid financing to help mitigate risks that constrained private-sector investment in badly needed infrastructure development, improvement, and expansion in developing countries. In seeking to develop an approach, DFID decided to bring in as many like-minded donors as possible so as to provide a single interface for both governments and potential private investors for the development and financing of infrastructure projects.

As a result, the Private Infrastructure Development Group (PIDG) was launched in 2002. The World Bank Group has been a member since its inception, first through the IBRD window and, since 2007, through the IFC. Current members are Austria, Ireland, Sweden, Switzerland, The Netherlands, the UK, and the IFC.

The Approach

Realizing that the in-house capacity in the capital markets sector ranged from limited to nonexistent on the part of most of the PIDG members, an approach was adopted that sought to draw on available private-sector expertise and experience with project development and investment.

At the same time, PIDG donors retain control of overall policy in order to ensure maximum developmental value and to limit any “subsidy” element to the absolute minimum necessary to mitigate risks that constrain private-sector investment. All donor members have a say on whether or not a new facility should be established under the PIDG umbrella, but those donors contributing to a specific facility lead the more detailed operational criteria for that facility.

The model that was developed was based on a standard commercial company approach, with donors setting investment policy and country/sector limits and the company’s board of directors making the decisions on individual investments within these policy parameters. Company equity is held by a trust fund established by the PIDG specifically



InfraCo Chanyanya Irrigation, Zambia

for this purpose, and board members are selected and appointed by a nominated committee representing participating donors. Project identification and day-to-day company management functions are contracted out to commercial management companies recruited by open competition.

In order to have a single interface with which the board could interact at the donor level and to ensure that all parties abide by the governing principles, the participating donors convene biannually as a Governing Council, which is serviced by a program management unit tasked with day-to-day management of the PIDG and the implementation of council decisions. The diagram below illustrates the overall approach.

Outcomes to Date

Using the above-mentioned approach, the PIDG has to date established three companies: The Emerging Africa Infrastructure Fund Limited (EAIF) to provide long-term hard currency debt; GuarantCo Limited (to provide local currency guarantees); and InfraCo Limited (a developer of greenfield investment opportunities).

In addition, the PIDG provides direct grant funding support to IFC's Infrastructure Advisory Services through a specially established trust fund at the IFC (the DevCo trust fund), which is used to pay for consultants who develop and take forward IFC advisory mandates. The PIDG also has its own technical assistance fund (TAF) for local capacity building for both the private and public sectors in association with PIDG projects.

Results

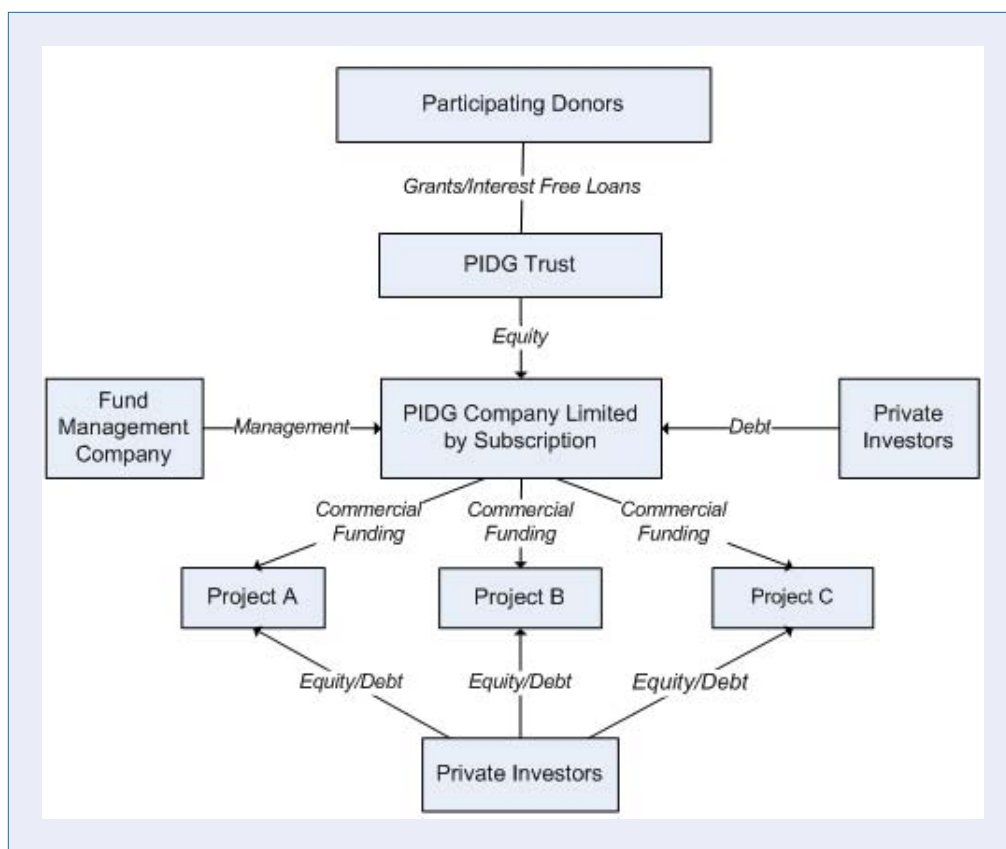
As of July 2009, the PIDG donors had jointly invested a total of \$334 million in all the PIDG facilities and operations. There were 30 projects to which loans/guarantees had been issued by EAIF/GuarantCo, plus 15 projects developed by InfraCo and DevCo, which had been successfully concluded with private-sector investors. These projects have included investment commitments of \$9.5 billion by the private sector, i.e. approximately 30 times the expenditure to date by the PIDG donors. (It also needs to be borne in mind that most of the PIDG donors' investment is in the form of equity through the PIDG trust fund, which is itself making a return.)

Lessons Learned

Over the seven years since PIDG established its first company, a number of lessons have been learned as to what approaches work in setting up donor-funded private companies in the development sector and the pitfalls that await those seeking to establish similar multi-donor mechanisms.

1) Nominate a single donor with the responsibility for the development of a facility/company.

EAIF was the first PIDG facility established (and therefore would generally be expected to take longer to develop). EAIF was initially developed and taken forward by DFID, with other interested donors "buying in" once the company was up and running. EAIF took two years to launch from inception to full operation.



In contrast, the next PIDG facility to be developed (GuarantCo) was initially developed jointly by two PIDG donors. After three years, however, the joint development approach was abandoned because working with two governments—each with different rules, regulations, and drivers—proved difficult. GuarantCo was eventually taken forward by a single PIDG donor, with others "buying in" on completion and was then fully operational within a year.

2) Manage donor expectations with care: It's best to underpromise and overdeliver.

In taking forward a new initiative, the project officer has an understandable tendency to use the most optimistic assumptions (often without fully spelling-out

the potential downside) in order to gain interest and investment from the donors. The project officer is faced with the twin problems of needing to forecast tangible results within the time scale of funding horizons (usually three years for bilateral donors) while operating within what is practical for a complex, innovative, and often untested initiative.

In the case of PIDG, the first initiative (EAIF) got off to a good start because of a backlog of projects seeking long-term debt but then stalled from a predictable lack of suitable bankable projects. EAIF made no new loans for almost a year while efforts were made to identify new investment opportunities. This led to donors' disillusionment, which was difficult to overcome once business picked up and further equity was required. In retrospect, it would probably have been better to highlight this potential problem from the outset, but this was not done in order to encourage initial investment commitments.

In the case of InfraCo, donors made it clear from the outset that they would be seeking high developmental returns from the initiative. In response, a concept was adopted that specifically targeted a number of projects that would generate high direct developmental returns (as opposed to indirect returns through increased growth). In practice, such projects have been difficult to develop, have taken longer than anticipated to bring to the point of sale, and are proving difficult to sell under current capital market constraints. The consequence is that donors are loath to increase equity inputs to InfraCo at a time when this is sorely needed, saying that they want to see results before making further investment. In retrospect, it would have been better to have made it clear to donors that, in order to achieve some early wins and thus demonstrate success, more straightforward projects (which would demonstrably bring quicker returns to investors) would be appropriate during the early years of the new facility.

3) Make clear from the outset that it is the company's board and not the donors who hold the responsibility for project selection.

During the early days, PIDG was "feeling its way" with the donors trying to take forward a concept (grant investment from aid donors in private development/investment companies) that was completely new to all involved. As a consequence, an arrangement

was initially put in place under which all projects being put to the companies' investment committees would be submitted to participating donors on a 10-day "no objection" basis. This system soon became a constraint to project development because the donors felt compelled to ask detailed questions about each and every project if they were to give their approval, and the 10 days became many weeks.

The donors were eventually persuaded to abandon the 10-day consultation period and to trust the decisions on project selection made by the boards, limiting donor (shareholder) inputs to holding the boards accountable for complying with the investment policy set by the donors.

Much friction and many delays would have been avoided if such a policy had been put in place from the outset.



EAIF Safel Roofing Project, Kenya

Conclusion

There are advantages to all concerned (donors, developing countries, and the private sector) by providing donor support for the development and funding of private-sector projects in infrastructure (and other) sectors in developing countries through multi-donor approaches such as the PIDG. Bilateral donors, particularly those with smaller aid budgets, are able to participate in and guide multi-million dollar investment programs; the IFC gains access to significant amounts of grant funding; and recipient-country governments and the private sector have a single interface with an experienced investment professional and a quick, non-bureaucratic, decision on an investment request.



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