

Sustainable Infrastructure Development – Role of the Private Sector

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1. Introduction

1.1 Sustainable Development

The core idea of sustainable development is development that meets the need of the present without compromising the ability of future generation to meet their own needs. In broad terms sustainable development encompasses:

- Help the less privileged, who for their sustenance and livelihood depend on the natural habitat, and tend to disturb the eco systems in the process.
- Self-reliance development.
- Cost-effective development – the development should not degrade the environment nor should it reduce productivity.
- The issues of health control, appropriate technologies, self-reliance for food, water, air and shelter for all.
- The notion of people-centered initiatives.

1.2 Sustainable Infrastructure

One of the major issues of sustainable development is provision of environmentally sound infrastructure such as water supply and sanitation, power, transport and telecommunications. Infrastructure has been the exclusive province of the public sector and the performance of various Governance entities has been rather dismal. Further, the demands on infrastructure has been ever increasing due to the following:

- Population growth
- Rapid urbanization
- Growth in Income of the average consumer.
- Decline in official development assistance (ODA), state assisted subsidies and initiatives.
- Ever increasing demand for environmental related funding.

With this increase demand and the inability of the cash-strapped public utilities to provide financial resources for development and private sector participation in infrastructure development, it becomes very important that resources for development are directed towards sustainable development. A judicious mix of choices, therefore needs to be exercised to maintain this delicate balance.

2. Publicly Operated Infrastructure

The performance of publicly operated infrastructure and utilities has been rather dismal with the result they are financially insolvent and not self sustaining, and don't meet the objectives, therefore. The following problems have been identified and apply at varying levels to various public services:

- Quality of service is dismal.
- The coverage of service is limited with very low scope for autogrowth.
- The services cannot cope with expanding population.
- Inefficient operation.
- Poor maintenance.
- Excessive wasteful usage.
- Poor cost recovery leading to financial problems.
- Low labour productivity and high labour cost.
- Poor management – inability to attract management talent and qualified technical staff on a dynamic basis.
- Needs substantial subsidization.
- Lack of clear regulatory responsibility.
- Environmental problems.

3. The Private Sector in Infrastructure Development

Due to the poor performance of publicly operated infrastructure and utilities and ever increasing demands on infrastructure, the governments have been convinced to seek active involvement of the private sector. However, there are several challenges associated with private participation.

3.1 Promise of the Private Sector

The promise of private sector lies in:

- Better management
- Better access to private capital

3.2 Challenges in the Private Sector

While the benefits of private sector are clear, the obstacles too are substantial. The public sector that invites private participation also faces risks. The challenges in private sector participation in infrastructure development are highlighted as follows:

- Investments are capital intensive, and rely on state support indirectly.
- The projects have long gestation period
- Long payback period
- Private Sector risks are as follows:
 - Demand may turn out to be low

- Tariffs may be too high
- Delays in construction
- Condition of infrastructure may turn out to be worse
- Higher costs
- Financial risks due to currency devaluation
- Legal risks in disputes.
- Political risks
- Risks faced by public sector inviting private sector are:
 - The procured service may be sub-standard
 - Cost may turn out to be too high
 - Public opposition – especially from labour unions.
 - Difficult to achieve competition
- Lack of adequate legislation for private sector involvement.
- Non enforcement of property rights and contracts due to lack of proper legislation
- Bureaucratic inertia.
- Lack of confidence in Private operator.
- Fear of Foreign Operator
- Reluctance to deal with labour problems.
- The private sector may show too little interest to ensure competitive bidding.

4.0 Private Capital Flows

The private sector capital flow for infrastructure has been increasing since 1990s when many developing countries began liberalizing their markets to facilitate the same. The share of private capital flow has almost doubled from about 40% in 1990 to 80% in 1996. Foreign Direct Investment (FDI) amounts to nearly \$100 trillion globally. FDI is more important to sustainable development as it is accompanied by transfer of technology and management skills.

The main drawback of private sector cash flow in general and FDI in particular is that they tend to drift towards high and middle-income countries with seemingly sound macro economic policies.

There is however some change lately with the foreign investment in developing countries being expected to grow at a rate of 7-10% per year as estimated by World Bank. The explanation being given for this projection is due to liberalization in the policies of corporate governance, technological innovation, capital mobility and growing financial integration.

Traditionally, Private capital flow has really not been flowing towards social and environmental sectors. This has been due to legal restriction against private sector involvement in public services monopolies. Further, without enforcement of environmental regulations, freedom to charge user fee and to raise tariffs to cover costs these sectors were not attractive to private investors, domestic or foreign.

Recent years have seen strong trends towards privatization of state-owned enterprises and public utilities. Further private sector participation is being encouraged to invest in sustainable infrastructure development. The perceptible change is, that the FDI has gradually shifted from resource extractive industries towards infrastructure which are more environmentally benign.

5.0 Options for Private Sector Participation

There is a wide spectrum of options for private sector participation in infrastructure and public services. The options reflect the variations of the respective role of the private and public sectors. The options can be divided into two groups and they are given as follows:

- i. That retain public ownership and include the following:
 - a) Service contracts
 - b) Management contracts
 - c) Lease arrangements
 - d) Concessions.

- ii That involve partial or temporary ownership of assets. This group includes:
 - a) Build, own, operate systems and their variations
 - b) Joint Ownership or mixed companies, where public and private Sector operate jointly
 - c) Sale / divesture to the business entities having more benign postures.

The wide range of options allows flexibility and thereby allow the parties to progressively move from less risky arrangements to more risky ones.

6.0 Mobilizing of resources from the Private Sector

In order to attract private capital and talent (technical and managerial) a series of economic, financial, legal and institutional reforms are necessary:

- Product macroeconomic management practices.
- Stable and convertible currency
- Enforcement of contracts
- Demonopolizing niche areas
- Overhauling regulatory framework
- Removal of subsidies
- Removal of barriers to foreign capital
- Allow tariffs to reflect costs.
- Allow repatriation of profits.
- Encourage foreign participation
- Strengthen local capital market
- Improve access to international capital market.

7.0 Conclusion

The most important lesson learnt from the past experience is that certain basic reforms (macroeconomic stability, convertible currencies etc) are fundamental to attract long-term investment; a near perfect policy environment is not necessary to begin with. This is because of three reasons:

- i. Few successful initial transactions help to evolve policies and allow reforms to deepen.
- ii. Even poor countries having difficult environment can attract private investment if rewards are structured properly. Investment of multilateral agencies enhance the comfort of the private investor.
- iii. There is a wide spectrum of options and arrangements available for private sector participation.

The international community can play a very important role in enhancing private capital flow, in helping poor countries in their initial critical steps and in promoting and sharing of experiences among developing countries. The World Bank is taking serious initiatives to reduce risks and leveraging FDI for modifying the procurement processes. It is also offering loans and other financial instruments to help private sector in developing countries.

The UN may play a catalytical role to encourage developing countries in adopting sound macroeconomic policies and outward looking growth strategies which would eventually attract private sector capital. UNDP through its public-private partnership programme can encourage governments to introduce regulatory regimes and contractual arrangements to share and mitigate risks in private sector capital flow.

Initiation of Global Compact, a networking organization, constituted under the auspices of U.N. is one such forum where the good practices adopted by the private sector are deliberated upon and the information disseminated for overall benefit.

Review of Private Sector Participation in Infrastructure in INDIA

Introduction

Indians still receive infrastructure services largely through public entities—usually part of a government department the Expert Group on the Commercialization of Infrastructure Projects estimates that India needs to invest \$115 billion to \$130 billion in infrastructure from 1996–2001, and \$215 billion in 2001–2006 (NCAER 1996).

The government also has established a high-level task force to attract investment—including private funds—to projects of national and regional importance. The task force is concentrating on developing expressways, adding lanes to national highways, and building five world-class international airports.

India has started to restructure government roles in power—particularly by separating operations from policy and regulation. This has occurred to a lesser extent in telecommunications and ports. In other sectors the process is incomplete or has not yet begun

Telecommunications

The entry of private operators into the telecommunications sector indicates great potential for competition and private investment. But market structure and license conditions have undermined incentives for large investments and new entry

Power

Despite government steps to introduce private sector investment in generation, the poor financial standing of most boards means that far fewer deals have reached financial closure than expected.

Urban Water and Municipal Services

Not many privately sponsored projects have yet reached financial closure in the water and sewerage sector, which is handicapped by inadequate revenues and a cumbersome institutional approach

Roads

Some projects, like bridge and bypass construction, and some stretches in the NH network have been privately financed, government has begun introducing tolls on newly expanded stretches of road, and the number of toll roads, bridges, and bypasses is steadily

increasing. The government is now upgrading the national highway network which includes the private sector participation.

Ports

The central government has adopted broad policy measures to open ports to private investors and operators. Some maritime states are also attracting private investments. The central government is seeking private investment in captive and other facilities, and state governments are seeking private investment, largely in new sites.

Airport

To set the stage for more private sector participation, the government is planning to lease operations at the Calcutta, Chennai, Delhi, and Mumbai airports.

Improving the Public-Private Interface

The increasing emphasis on private provision of infrastructure services is placing new demands on the public sector's contracting and supervision skills. This situation frequently results in the bidding of projects that need more preparation. It, however is an acknowledged fact that here is a need for greater interministerial coordination at the central and state levels for pushing the desired reforms.