Public private partnerships and the provision of rural transport services in developing countries

by M J Witkiss, J L Hine & S D Ellis

Draft Report

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Draft Report

PUBLIC PRIVATE PARTNERSHIPS AND THE PROVISION OF RURAL TRANSPORT SERVICES IN DEVELOPING COUNTRIES

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CONTENTS

Abstract

This report reviews literature on Private Public Partnerships (PPP) that is of most relevance to the transport sector of developing countries. The role of a PPP arrangement to assist with the provision of rural transport is also considered. Issues such as competition, privatisation, regulation, contracts, the sharing of risk, finance, tariff setting, subsidies, the role of build, operate and transfer (BOT) schemes, competitive tendering and the setting up of a PPP are examined. An annotated bibliography is included in the Annexes of the report and additional material is presented on UK bus deregulation, cartel policy, downsizing and retrenchment, and the buying out of capacity.

1. INTRODUCTION

The term Public Private Partnership (PPP) refers, as the name suggests, to a project partnership for service or product provision between a public entity and a private concern (individual or group), and can occur in any industry or sector. They are set apart from other types of project or method of provision by exhibiting flexible management and financial structures.

PPPs are characterised by being flexible in all aspects so that they have the ability to adapt and be tailored to meet the specific conditions of each individual situation or circumstance. This flexibility means that the identification of an unambiguous or standard definition is at best difficult, but it is possible to identify common features that should prevail in any such project. PPP approaches range from conventional finance and delivery to fully privatised toll roads at the other extreme. (Lockwood 1997).

During the last few years there has been an increase in interest in finding ways that can combine the advantages of the public sector (i.e. community interest and control) with the private sector (notably efficiency and access to private finance). In the provision of transport infrastructure the interest in Build, Operate and Transfer (BOT) or Design, Build, Finance and Operate (DBFO) the desire to tap into alternative sources of finance has been of particular importance, especially given the fact that there are ever increasing demands on ever decreasing budgets.

"There is growing recognition across the political spectrum that we must mobilise the resources of the private sector if we are to build the transport infrastructure of the 21st century. To rely on the already over-burdened public purse...will mean serious delays." (John Watts, 1995)

The case for PPPs for highway development is made by Lockwood (1997) in a paper entitled "Public private partnerships are the answer: what is the question?" He suggests that finance and institutional roles are inextricably linked. Over time, legislation and regulation in the United States have begun to specifically encourage the commingling of toll and other public and private resources in cost-sharing arrangements with private road development entities. In addition it has permitted new forms of project delivery such as turnkey development, and established new frameworks for programme finance such as infrastructure banks.

In developing countries the case for PPP arrangements appears strong given the fact that budgets are far tighter and public sector debt represents a major drain on resources. It is commonly agreed that private firms can usually provide lower production costs, greater efficiency in service delivery, as well as having a greater capacity to maintain capital equipment (UNDP 1998). The UNDP also notes the fact that financial burdens on the government are reduced for wages, operating costs, debt servicing, and investment. However in setting a PPP arrangement, it is important to recognise and accept the complexity and time consuming nature of the process, that extensive government support may have to be provided, and that rates of return which commercial lenders and private sector equity investors will expect may be high. Augenblick & Custer (1990).

The PPP programme that the UNDP currently operates has been set up under the premise that the experience of privatisation in developing countries to date indicates that private corporations, NGO's and informal sector enterprises have potential advantages over government agencies in providing some types of services.

With respect to applying PPP to infrastructure provision, Heggie (1991) suggests that the introduction of commercial cost-accounting systems can reduce the cost of main road replacement by between 5-15%, while sub-contracting for road maintenance can be shown to reduce them by a further 20%. Because it is generally accepted that public agencies operate 'better' when faced with an element of competition World Bank policy has been to commercialise or corporatise public-sector agencies. This should ensure market discipline, hard budgets, clear objectives, and sufficient managerial autonomy.

Although a privatised firm may participate in a PPP arrangement privatisation itself does not necessarily imply a partnership. In a PPP the state does not relinquish all control over service or product provision, but can still tap into the advantages associated with private sector participation. Given that many PPP projects in developing countries are centred around public service and infrastructure provision, PPP arrangements are more beneficial considering that the service is often, in effect, a national utility. There are examples of projects in infrastructure provision, water supply, sanitation processing, telecommunications, urban transport, and road maintenance to name a few. For further, more detailed case studies, see Annex 2.

A PPP project could provide a solution to the problems of rural transport services in many developing countries. The Malmberg-Calvo report for the World Bank (1998) examines transport issues for rural villages in Sub-Saharan Africa. She notes that 87% of trips made in rural Africa are made on foot, with 65% of household time and effort being spent on transport. Furthermore, 70% of Africa's population live in villages, and the local transport network carries a third of the region's GDP. In view of these data there is considerable in finding new ways and methods of improving access and mobility.

There is increasing evidence that rural transport services that are currently provided in many rural areas of developing countries – particularly in Africa -are unsatisfactory. Service frequency is usually very low and, often effectively non existent for the local communities, even for areas that have relatively good road access. Although low incomes and the low density of demand are the main factors inhibiting the provision of better services there is much evidence of high transport charges, inefficiency and the operation of cartels. Given tight state budgets, the relative efficiency that the private operators are capable of, and the need to maintain service frequency and inhibit the worst characteristics of cartels a PPP project could represent a solution to the problem.

The purpose of this report is to review the literature on PPP that is most relevant to the transport sector of developing countries and to propose a possible PPP project to assist with improving rural transport services. The following Sections contain a review of the key issues relating to PPP and an annotated bibliography relating to PPP is provided in Annex 1. PPP case study material is provided in Annex 2. A possible rural transport project is provided in Sections 6 and 7. Using case study material from the UK and elsewhere a number of critical issues that are most relevant to the rural transport project are considered in Annexes 3 to 6.

2. PPP CHARACTERISTICS

The very nature of Private Public Partnerships means that no solution will be exactly the same as another as it will have been applied to meet the specific needs of a particular situation. But there are certain themes one can identify that will be present in all PPP projects. These are discussed below.

"The restructuring of agency and private entity functions in the delivery of highway facilities and services is generally known as "public-private partnerships", which can be defined as a change in roles and relationships based on a new mix of complementary public and private resources (expertise, technology, finance) pooled toward a common objective – while still achieving the partners' respective separate objectives."(Lockwood, 1997).

As the name suggests, partnership is central to the PPP operation. The partnership and co-operation will involve all parties that run the project and, of course, all parties will be affected by the project. This will include local participation through community groups, local business and any other interested party. Kerf & Smith (1996) note that it is vital to involve all parties in dialogue, cross-sectoral issues and options assessments, and the mobilising of local finance.

The PPP will be set up with specific goals and objectives, and then tailored so that the said goals and objectives can be met. The common view is that clear and decisive goals will make operation a lot easier and also ensure that all parties are aware of what to aim for. A "win-win" objective is seen to be the general motive.

PPP's provide an alternative to full privatisation in which government and private companies assume co-responsibility and co-ownership for the delivery of services. Through these novel partnerships, the advantages of the private sector - dynamism, access to finance, knowledge of technologies, managerial efficiency, entrepreneurial spirit - are combined with the social responsibility, environmental awareness, local knowledge, and job generation concerns of the public sector. UNDP 1998.

Heggie & Vickers (1997) note general characteristics of PPP, and see them to include the following: explicit contracts, ownership and responsibility, enterprise accountability and financial discipline, adequate and stable flows of funds, sound business practice, and the goal to achieve a "win-win" situation. Perhaps the most important factor here relates to enterprise accountability.

For successful PPP it is essential that the operation be subjected to rigorous economic and financial appraisal on a regular basis, and that it operates on commercial principles. Soft budgets and a lack of auditing needs to be avoided. If not the firm will have a tendency to revert back to the main problems associated with public sector service provision.

From the above key words can be identified to describe a PPP. They are partnership, commitment, stability, accountability, transparency, and local participation. Thus PPPs have the advantage of being able to employ the private sector (for finance and efficiency), without having to compromise all control over the operation as can often be the case with full privatisation.

"Public-private partnerships – transactions in which the private sector brings its expertise and resources to bear in public sector projects. While the form of the arrangement varies, a common element to all such partnerships is that the partners' objectives are aligned towards successful completion of the venture. The private and public participants thus work co-operatively to achieve their mutual goals: a team approach producing a win-win solution for all concerned." Shaw-Pittman, 1998.

In a Public Private Partnership the efficiency and financial resources of the private sector works hand in hand with the social and economic considerations of the public sector. Projects are successful when the parties work with each other and share with each other their individual attributes to meet a common goal. Hopefully the flexibility that this operation offers means that there should be minimal risk of mis-identification of potential projects, as each operation is tailored to conditions in its locality.

Within the transport sector a variety of forms of public/private co-operation have been adopted for many years that have many of the characteristics of a Private Public Partnership. These include leasing, franchises, and concessions, (although the term "concessions" is applied to all three). For all three of these procedures an agreement is reached defining objectives and allocating risk. Specific rights and obligations are granted to the company, which are specified in terms of time and geographical area. With a lease the operator leases equipment to supply the service. With a franchise operators provide services that are fully specified by the franchise authority and may be responsible for some investment. The franchising authority may control for common functions like marketing. With a pure concession (such as the Build, Operate and Transfer BOT arrangement) the operator covers investment costs and more commercial risks. Concessions are reported to have been used in 18 countries for bus operation, 12 countries for passenger rail, 8 for freight rail, 29 countries for road projects, 23 countries for ports and 25 countries for airports. (Shaw et. al. 1996).

3. THE ROLE OF GOVERNMENT

There is a very clear pattern that emerges from the texts regarding the chronology of PPP lifecycles. Authors are at great pain to emphasise that some processes can take very long periods of time to conclude, and it is essential that they are not rushed or ignored. At the beginning, there is a heavy onus on the government to ensure that the right project and private company are selected. This may require detailed financial, economic, environmental and social assessments. Careful consideration also needs to be given to the tendering process itself to ensure that the contract will be mutually beneficial whilst still allowing the original aims and objectives to be met.

3.1. The Wider Political, Legal and Economic Environment

To ensure the success of any new organisational structure it is imperative that the wider political, legal and economic environment is favourable. Because of their often unique and complex nature Private Public Partnerships may be more dependent on these external considerations than more traditional forms of economic organisation.

Most economies will not progress without a stable political and economic environment. Respect for the rule of law and property ownership rights are essential. In addition contracts should be legally enforceable. Governments must recognise that they too should be subject to the rule of law and that they, as with other parties, are subject to contract law. Hence they cannot arbitrarily change terms of an agreed contract when it is convenient. Many authors that have reviewed economic developments in the former Soviet Union and countries in Eastern Europe have stressed the need for a proper legal framework. The correct form of institutional and legal framework that can facilitate economic progress can so often make a difference between success and failure.

In order to ensure success at every level of implementing PPPs a high degree of political commitment is paramount. Senior politicians may need to take on the role of "champion" to ensure the success of large and complex PPP. A host of issues may need to be tackled including the wider political agreement, changes in legislation, government finance, labour relations, relations with the rest of the commercial sector etc.

It is much more likely that a PPP will be successful if there is a thriving economic environment and the future demand for the services of the PPP is secure and growing. Access to private finance has been highlighted as a major advantage of a PPP hence it is important that the banking sector is well developed and that there is ready access to financial markets. Local stock markets can of course assist in this respect. Recent events in the Far East have highlighted that currency risks will remain a particular problem for many developing countries.

Many PPPs have been set up after denationalisation and they may operate as monopolies or cartels. Although specific regulations relating to the PPP or industry may be in place to control or curb the monopoly power some form of control may exist through standard anti-trust legislation. However it is recognised that for most developing countries legislation is generally weak in this area.

3.2. Project Selection

3.2.1. Financial and Economic Feasibility

Within a liberal market economy government intervention in a sector usually arises because of a recognised market failure. Factors such as the lack of competition arising from monopolies or cartels, important externalities, imperfect information, increasing returns to scale and particular problems with charging are common reasons (Carbagio, 1993). Private Public Partnerships naturally involve a substantial amount of government intervention and therefore these same criteria should be present, however other factors also apply. Because the private sector is involved in supplying the service of the PPP it is essential that the project can be profitable.

It is important for the government to commission a financial appraisal for all Public Private Partnerships to ensure that they will be profitable and to understand the key factors that will limit their profitability. PPPs can take a wide variety of forms and for each form different considerations might apply. For example for a major national project such as an interurban toll road it is essential to undertake a full separate economic appraisal of the project. Because of the length of time involved in setting up a PPP (particularly if legislation, compulsory land purchase or a planning enquiry is required) it important that the economic analysis reflects this.

For a small urban or rural based project a full separate economic analysis may be inappropriate. For a locally based PPP criteria such as local interest and likely local participation by both the public and private sectors and the wider community may be critical.

3.2.2. Poverty

The effect of the project on the poorest sections of the community are important and a conventional economic or financial analysis will often overlook this. If necessary a study could be undertaken within the framework of an urban or rural 'livelihoods' approach. Opportunities for improving local services and conditions and the potential for technology transfer and capacity building will all be important considerations.

Different measures can be taken to ensure that the poor can benefit from a PPP. Blanket price subsidies nearly always benefit the richest sections of the population who tend to make the greatest use of nearly all services. For transport services there are few readily accepted, simple mechanisms to ensure that the poor will get the greatest benefit from a subsidy. Although it is argued that the most effective solution to help the poor might be to make adequate budgetary allocations to poor regions for infrastructure provision (e.g. World Development Report 1994) this approach will often lead the provision of roads but it does not guarantee that vehicle services that the poor can use will be provided. To overcome this perhaps the targeting of subsidies to transport services operating in the most remote and poorest locations may be the simplest approach.

3.2.3. Environmental Assessment

Many donors and governments will also demand that an environmental assessment of the project should be carried out. For transport projects safety is, of course, extremely important and a separate safety audit of the project may be required. For the more crowded urban environments transport projects, noise and air pollution may be important issues to consider. For rural transport projects the effect on the natural environment can important particularly if the project affects fragile environments such as forests or wet lands.

3.3. The Design of the Private Public Partnership

In designing the form of the PPP the following questions need to be answered:

a) What is the overall goal of the PPP? How will it benefit the national and local economy and the livelihoods of those affected. How can this goal be formulated to produce a common interest between the provider and the public interest? Will both parties perceive the partnership as a 'win-win' solution?
b) What institution will represent the public interest? Is it an independent authority (i.e. a 'watch dog' or regulator), a government ministry, local government, a community based organisation?
c) What current and new institutions will be involved in providing and regulating the PPP service? What new legislation will be involved in setting up these bodies? How will the private operators be selected? How will the personnel be selected to run the public bodies?
d) What is the size and duration of the project?
e) What exclusive rights will be offered to the operator?
f) How will provision and regulation of the PPP be initially financed? Is any external aid funding required? How will revenues be generated by the project? Who will own the major assets of the providing service? Is any transfer of assets planned?
g) Are there any complications such as compulsory land purchase or planning enquires required?
h) What are the major risks involved?
i) What will be the contractual relationship between the provider and the Government (or its appointed body)? In terms of the contract are the risks allocated to the party best able to manage these risks?
j) What selection criteria are to be applied to the service provider? Is the provider going to buy the rights to operate (as in profitable operation) or is the government going to pay the provider because other wise it would be unprofitable? Are tariff levels or subsidies to be specified in the bid? Are minimum levels and quality of service to be specified? How are tariffs to be controlled? If the public sector imposes changes to the detriment of the provider (e.g. price controls) is compensation or other financial support specified?
k) What reporting requirements are involved?
l) Will independent monitoring performance take place, who will do it and what form will it take?

m) What will be the form of regulation and what sanctions will be involved for non-compliance?
n) How will disputes be settled between different parties?
o) Is any external technical assistance going to be required to set up and run the PPP?
p) Are any special tax privileges envisaged.

It should recognised that the costs of setting up PPP in terms of feasibility studies, bid preparation and setting up monitoring systems are not trivial. For example the transaction costs could amount to between 5 to 10 percent of the project costs (Kerf and Smith, 1996).

Most authors recognise the importance of clear consistent objectives and a commitment to commercial principles as important characteristics of success. Public sector bodies particularly suffer from a lack of autonomy and may lack accountability. Financial problems may emerge when tariff adjustments lag behind cost increases. Problems with wages and employment occur when the public sector is used to create jobs (World Development Report, 1994). It is important that new PPP arrangements do not suffer from the same problems.

In designing a partnership project it is important to recognise that conflicts and tradeoffs will arise in the pursuit of different subsidiary objectives. Inevitably some compromises will have to be made. For example for a new infrastructure project there may be a compromise between the desire to maintain and enforce low tariffs and the desire for competition. If the private partner believes that there will be little competition then, perceiving that risks are lower, he may well agree to accept lower tariffs. Similarly if regulations governing the PPP are perceived to be very restrictive then the greater the likelihood that higher tariffs will be demanded. Likewise there may be a tradeoff between the government's loan guarantees and the commercial financial cost of a project.

Sometime multiple criteria can be reduced to a minimum by incorporating some objectives as standards (e.g. bus under a certain age) at the prequalification stage and as conditions of contracts.

3.3.1. Project Size and Contract Duration

Large projects generate scale economies but may reduce competition. Small projects may increase the number of possible companies that could compete for service but may make integration more complicated. A number of small projects will also increase the management and bidding costs compared with fewer large projects. While the term of a bus project may be only three years road infrastructure may be as long as thirty years. The longer the contract period the greater the chance of 'regulatory capture'. (Shaw et al. 1996)

When planning the duration of a project the economic life of the assets provided by the private company need to be considered. Problems arise if the duration of the contract is much shorter than the economic life of the privately provided assets unless the assets are divisible and viable in alternative uses. Motor vehicles are easily deployed to other routes but a lot of other machinery is less easily moved and transferred.

3.3.2. Award Criteria and Renegotiation Terms

Award criteria together with the relative weight attached to each aspect need to be defined at an early stage in the development of a PPP. The bidding process must also be transparent so that risks of allegations of corruption can be minimised. To reduce the government's exposure to risk pre-qualification criteria are often established.

Different procedures can be adopted for the renewal of a contract (Shaw et al, 1996):

a) There can be automatic renewal if performance has been acceptable.
b) The existing operator can negotiate a roll-over which maintains continuity of
   service and avoids the retendering process.
c) The existing operator can be bought out by the government that pays for the undepreciated assets.
d) Rebidding. If the existing operator is unsuccessful they receive the value of their bid from the successful bidder's offer. The government receives the balance and the value operation is set by the market.

3.4. Competition and Regulation

During the last two decades privatisation has been a popular way of introducing commercial principles and efficiency to public monopoly services. Although privatisation will usually increase efficiency there is a need to ensure that the monopoly power is not abused, the infrastructure will be maintained and the benefits passed on to the consumers. This is achieved through a detailed system of regulation.

Where privatisation of a public monopoly is being considered the unbundling of services is another solution that can provide benefits. By isolating the natural monopoly segments of an industry (e.g. separating the rail track from running trains) unbundling promotes new entry and competition in segments that are potentially competitive. The lateral unbundling of transport services (e.g. splitting off different bus routes) can lead to a reduction of cross subsidisation between the routes. While many believe cross subsidisation is not to be recommended in many policy areas (some services are made unnecessarily expensive and others are provided which might be not be viable) within the transport sector care needs to be taken to ensure that poorest sections in the more sparsely populated areas are not adversely affected.

Other methods to encourage competition are:

a) competition from substitutes or between modes. For example to allow minibuses to compete with conventional bus services.
b) competition between different groups. Within a licensed public transport franchise system competition can be promoted by encouraging competition on common sections of the route. This form of competition enables the public sector to control the supply to some degree and can limit anti-competitive behaviour.
c) competition in infrastructure markets. Although numerous suppliers in infrastructure are rare, competition amongst a few rival suppliers can

lower costs and prices and thus limit the risk of monopoly abuse. Many good examples of new forms of competition in this area come from the telecommunications sector with the advent of cellular phones and from power generation.

d) competition for the market. Where direct competition is not possible efficiency can be increased through a contract to supply the service. Competition occurs before the contract is signed and when the contract is up for renewal. The procedure provides an alternative to replying on a detailed regulatory apparatus. Examples include both leases, where the government supplies the infrastructure and the contractor the right to use it, and concessions, (such as a route franchise) where the contractor has responsibility for the investment. (Sustainable Transport 1996)

The weight of evidence suggests that competition in or for the market for services is more effective in responding to consumer demands than are mechanisms for making public enterprises more accountable (World Development Report, 1994). Similarly the adoption of commercial principles is impossible to sustain unless they reflect a wider political commitment to improve public sector delivery.

The main purpose of regulation is to ensure safety, control monopoly power, provide environmental protection and guarantee service frequency and quality standards. Many aspects of regulation will cover the whole country and may relate to many different industries beside the transport sector. Commercial organisations will be subject to a wide range of general legislation including health and safety at work, employment, pollution and the environment etc. General anti-trust and restrictive practices legislation may also exist. For a particular Private Public Partnership in the transport sector specific regulations are most likely to relate to those economic aspects covering aspects such as tariffs, investment, maintenance, commercial entry to compete in the market and service frequency and quality.

A new regulatory authority may be required but it is also possible that a multi-sector agency can be used. This would help share the costs and resources. It may also reduce the vulnerability of the agency to local 'capture' by the industry and reduce vulnerability and improper political interference. It can also reduce the risk of inconsistent approaches between sectors. (Kerf and Smith, 1996)

Most authors argue that regulations should be as clear as possible, and that regulators should be well informed and have sufficient resources to do their job and as far as possible be independent of political control. It is also argued that there is a balance between too much regulation and too little. If regulation is too severe then flexibility of the provision of services in response to changes in the market will be adversely affected. Too little regulation can lead to unsafe operating practises and that powerful operators and cartels may pay little attention to the needs of the community. Mitchell & Botha (1987) argue that because it is harder to re-impose regulation at a later date care should be taken to ensure that regulations are not initially perceived to be lax.

Once the contracts for a PPP have been agreed and the project is underway the government then takes a role of observer and monitor, to ensure that the contract requirements are met and that the project is on course. Throughout the lifecycle of a PPP contact is regular with steering and advisory groups (that can also include experts in the field and representatives from international and donor agencies) taking meetings to discuss project progress, and any amendments or changes that may need to be made. The flexible structure of PPP should allow it to adapt to changing circumstance over the period of the project. Adjustment is a key quality to have, and the role of the group as a whole will be to identify problems and act swiftly and efficiently to deal with them. The goal should be to move the project forward all the time, to develop it so that it strengthens its position and develops further than originally intended if at all possible.

3.4.1. Setting Tariffs

One of the most important area of regulation, after the PPP is set up, is tariff setting. It has been very common in many countries for tariffs for a wide range of services to be held down (i.e. well below the rate of inflation) for political reasons. The result has often been very poor service provision because of the insufficient revenue to pay for adequate investment and maintenance of the services. It is important that if a new PPP is to be set up that the forecast revenues are adequate to pay for the long run costs of supplying the service. There are various formulas for up rating tariffs with inflation. For some industries with strong technical innovation or reducing costs (e.g. power and telecommunications) for price capping formulas based on inflation minus 'X'. Another approach is to determine tariffs on the basis of rate of return calculations. Whilst this approach does have merits (particularly if changes in component prices are very substantially) it is usually much more difficult than is often envisaged at first. It may become highly dependent on rather doubtful data and, in the long run, it will provide little incentive for the operator to control costs.

If forecast tariff revenues are inadequate to cover the long term costs then it should be made explicit at an early stage as to what other funding will be made available to cover the shortfall. The interest of the private partners to a PPP agreement will of course be adversely affected if they believe that tariffs and hence revenues will be inadequate.

3.5. Financial Viability and Risk

The financial viability of a PPP over its life must be sufficient to service the project debt and to provide a return on the equity that is commensurate with the long term risks of the equity investors. Sometimes governments are surprised at the implicit rate of return expected by a project. Foreign investors may well be looking for rates of return in the range of 18 to 30 per cent. In order to assess a particular bid it is important to take as comprehensive a view as possible of the total nature of risks involved. In assessment it is also important not to loose sight of the potential benefits (i.e. terms of cost reduction, new investment and better management) of private involvement in a PPP compared with other forms of institutional arrangement. Obviously the more guarantees the government can give the lower the necessary rate of return to compensate. The government's past track record in meeting its other commitments will, of course, be critical in this respect.

Where subsidised transport services are planned different approaches are possible to distribute the revenue risk between government and operator. With the ***gross cost*** agreement the government retains all revenues collected and pays the operator to run the service. With the ***net*** or ***minimum cost*** agreement the operator retains all the revenue it collects and pays an agreed ***top up fee***. In the former case the operator carries the cost risk but the government carries the revenue risk. While in the latter case the operator carries both the revenue and cost risk. Experience from the UK has shown that the gross cost agreement attracts more concession bidders, particularly small firms than the net cost agreement. Because of the increase in competition ***gross cost*** contracts have been found to be less costly to the government than ***net cost*** contracts for a given service. (Shaw et al. 1996).

Many have argued that private finance may not provide the cheapest financial solution and that it would be better for the government to provide finance itself. Although this may be a valid argument it does depend upon the overall national debt servicing requirements of the country. If the country contemplated paying for (or guaranteeing) a number of very large projects then the cost of national debt servicing could rise substantially. One of the reasons for the lower government borrowing rates is that the risk are reduced because the government has recourse to taxation. In fact raising taxes is not costless in terms of use of resources and the distortions to the rest of the economy. It may be argued that the total social costs of raising finance in this way may be similar to or higher than for private finance.

There are a variety of risks associated with a project. Some risks are within the control of one or more of the parties to the project. The conventional wisdom is that each risk should be assumed by the party within whose control the risk lies. Other risks are outside any party's control but they are insurable, still other risks are uninsurable.

For infrastructure projects usually a higher risk is recognised during the construction phase and a lower risk during the operating phase. The risk that the project will be completed on time to a fixed price is usually assumed by the construction company and secondarily by the project company. The risk that the project will not perform as expected is usually covered by warranties from the construction company and its suppliers, as before, there is an operating risk secondarily assumed by the project company.

The risk of interruptions to cash flow are usually the responsibility of the project company however lenders to major projects will usually demand standby finance arrangements. Commercial insurance to cover this is also possible.

Inflation and foreign exchange rate risks are totally outside the control of the project company and usually the government will be asked to go some way towards covering these risks. Period price adjustments may be allowed based on a relevant price index. Similarly convertibility at an exchange rate may be required to cover external debts. Arrangements to achieve these guarantees will vary.

Standard risks such as third party liability, casualty and workman's compensation insurance are easily insured. However some risks (usually classified as 'force majeure') are uninsurable or not insurable at a reasonable cost. The equity investors may assume some coverage for these risks but cannot provide cover to the project's lenders. Lenders may require that host governments provide some coverage for these risks.

In order to reduce the overall cost of the project the government may adopt a variety of financial and other support mechanisms to the project. Guaranteed revenues, provision of assets, different forms of loans, the purchase of the project company's equity, and the introduction of specific regulations (e.g. protection from competition) are examples. (Augenblick and Custer, 1990).

4. THE ROLE OF THE PRIVATE SECTOR PARTNERS

4.1. Participation in the Initial Planning of the Partnership

Although the public sector will usually have the greatest responsibility for planning and putting together the partnership this is not carried out in vacuum. It is both likely and desirable that considerable consultation takes place between the government and representatives of the most interested private sector organisations. Although plans can be changed at later stages it can usually save a great deal of time if consultation can take place at the early stages of a project. This should help to weed out 'non starters' and help to shape the project into a form that is most likely to be successful in the long run. These issues become even more important if there is an international aid dimension to a project. There is usually considerable inertia associated with international projects and, coupled with the inevitable communications problems, this reinforces the need to ensure that a successful shape to a project is identified early.

It has been suggested that the initial contribution to feasibility studies is an indication (along with other markers) of the likely private companies that should be selected to participate in the partnership.

4.2. Organisational Capability

Before a private sector organisation can agree to be considered for a partnership it needs to consider its capabilities, strengths and weakness' in providing the service for the areas identified for the partnership. As with all new ventures an assessment needs to be made of its managerial experience and capability, its technical knowledge, the physical resources of buildings plant and equipment, and the financial strength of the company.

Bennathan & Thompson (1992) highlight the fact that in less developed economies, because of gaps in their knowledge, management may not be sophisticated enough to deal with a new market situation. They point out that this can be easily rectified, and that over time (as the PPP develops) managerial and institutional capacity should improve.

Where weakness are identified then steps can be taken to enter into agreements with others, buy in new capacity or even raise the matter with the public sector representatives as a candidate for possible international aid.

4.3. Finance

It has been identified earlier that one of the major strengths of the private sector is that it can bring in the resources of external finance. Clearly discussions will need to be held with banks, and other associated firms on the best way of raising the necessary financial resources. The nature and composition of the new funding required will, of course, be dependent on the main needs of the project (i.e. are the costs predominantly domestic or is a substantial amount of foreign exchange required?) the capabilities of raising money on domestic market or international market, the financial time profile requirements and the nature of the principal risks (see Section 2.2.5).

For most PPP projects that have a strong local or social dimension, revenues will be principally generated in local currency while often a significant component of the initial costs may be foreign sourced. Convertibility, inflation and exchange rate risks can therefore be important considerations. Many developing countries, particularly in Africa have relatively inefficient local financial systems. Credit has often been allocated on the basis of political influence rather than on the basis of market returns. In many African countries, if substantial sums are required, it is likely that some form of foreign sourcing may be involved. One encouraging development has been the recent growth of local stock markets in developing countries. It is forecast that the growth in Sub-Saharan markets could expand by a factor of five by the year 2010. In time these will help with providing local equity (Kerf and Smith, 1996).

4.4. Attitudes and Values

Within the private sector there is, of course, continuous pressure on managers and staff to perform productively and, to ensure the survival of the company, to produce a profit. This pressure is greater when the company is subject to strong competition. When the company is a monopoly the pressure is usually much reduced. In common with state organisations, the staff of private monopoly suppliers that have a degree of high job security will often be less concerned about the quality of service they provide. Where the Private Public Partnership is effectively a monopoly, thought should be given as to how to motivate staff to work efficiently and provide a good service.

Public sector firms all over the developing world are characterised by overmanning. In addition staff wages are often lower than in the private sector. (It should of course be noted that this is not necessarily the case in high income countries. Many public bus service operators in Europe offer much higher wages than private operators and that this can represent a major financial benefit - for the taxpayers and customers- of privatisation.) One obvious solution for the privatised company to the problem of inefficiency and poor service provision is to reduce staff levels and raise wages. The staff must, of course, be made aware that greater demands will now be made from them in exchange for the higher wages. Assistance from the government will usually be required to fund public sector retrenchment policy.

In setting up the management structure to work in the new partnership it is important to fully accept the values and ethos of the new PPP arrangement. It is likely that the internal affairs of the company will require a greater degree of transparency than may have been normal in the past. The PPP may well require the reporting of much information on the performance of the company.

Successful commercial enterprises in high income countries that have a high public profile now invest heavily in training staff in dealing with the public, and to provide a good service. The evidence is that such training does promote a positive change of attitude that is both helpful for efficiency and staff well being, and promotes loyalty to the company and its goals.

Many private companies have been criticised for taking a short term view. This can manifest itself in not maintaining capital assets. In part this may be reflection of the contractual terms of the relationship or the uncertain nature of the economic climate; it may also be symptomatic of general management attitudes. If necessary contractual arrangements and staff attitudes should be examined to ensure that a long term view is taken both for the long term company survival and the good of the PPP.

5. SOME LESSONS FROM RUSSIA AND EASTERN EUROPE

There is now a substantial amount of literature on the experiences of privatisation relating to former communist countries. Much of this material is relevant to the problems and failures that may occur with the setting up of Public Private Partnerships in developing countries.

In an examination of the problems encountered with the Russian Mass Privatisation Programme (MPP), studies by Boycko (1995) and Bennathan & Thompson (1992) have shown that in most cases the legal and regulatory frameworks will require substantial modification for efficient private sector operation to occur, and that rapid and ill-thought-out reform has lead to major problems.

In Russia "re-profiling" has become a particularly important issue. Here private firms that had been given contracts to operate a service simply changed their activities to fit their own personal business motives. This often resulted in failure in service provision, price hikes, and tension between the interested parties. This all occurred because of loopholes in contracts that meant that nothing could be done to prevent the re-profiling. The wider economic chaos that reined in the region at the time did nothing to help matters as private firms often found it difficult to stick to original service agreements and had to change in order to survive. Vacroux (1995) notes that in the Primorsky Krai region of Russia, the competitive tender process incorporated conditions that prevented the new owner from changing the line of business for a period of five years.

The Webster & Sheppard (1994) study of private sector development in Russia warns that new private firms, if left unchecked, have tended to have a 'quick-buck', short-term outlook. This may or course be a rational response to perceptions of the wider macro economic problems of the country. In contrast the state owned enterprise tended to look to the longer term and be a better guarantee of service delivery but lacked the flexibility and adaptability of the private firm. An arrangement that combines the advantages of the private and public sectors such as a PPP may be the best solution. The study recommends that to improve the situation it is desirable to remove any constraints to business development, by identifying and ranking them, and then addressing those with the highest degree of occurrence.

The study of road haulage conditions in Central Europe by Bennathan & Thompson (1992) indicates that depressed economies often accounted for excess capacity in the industry. This indicates again the importance of economic and political stability for the success of private ventures. They also note that policies that leave firms to get on with adjusting by themselves will not induce the necessary changes in operational behaviour, and response to competition to operate effectively. Mechanisms for change need to be explicit and well recognised and an institutional body is required to implement the reform programme. Legal frameworks can often be the difference between success and failure.

They also note that the changes that occurred have left the transport industries virtually free of regulation, but that there is a definite need for government to fashion instruments of economic control. This indicates an advantage for PPP over full privatisation, as under PPP government can retain a wider range controls and monitoring facilities to ensure that the project is operating the predetermined goals.

6. THE PROVISION OF TRANSPORT SERVICES IN RURAL AREAS OF DEVELOPING COUNTRIES

6.1. Existing Problems

The PPP approach could be used to help solve the problems of providing rural transport services in Developing Countries –particularly in Sub Saharan Africa (SSA). Currently many African Countries suffer from very poor service provision and high transport charges. Although most services are provided by the private sector vehicle utilisation is low, cartels are common and government regulation is weak. In this section key problems are identified which might be solved through various forms of intervention.

The following key issues have been identified as the major constraints on the satisfactory development of rural transport services (Ellis & Hine 1998):

- Low density of demand for transport
- Poor quality infrastructure
- Poor diversity of vehicle types
- Uncompetitive transport markets
- Lack of understanding by government donors and other agencies of the potential benefits of increasing the efficiency with which transport services are provided.

Taking each in turn.

6.1.1. Low Density of Demand

This is the single largest obstacle to the improved provision of rural transport services in Sub Saharan Africa. Although transport demand is largely outside the control of government, measures can be taken to maximise effective demand of transport services. Measures could be taken such as the increased provision of rural markets, ensuring that road networks have at least a minimum degree of interconnectivity to reduce dead end routes, make greater use of transport brokers to match vehicles and loads and use modern communication devices such as radios and telephones to link isolated areas to centres with vehicle services. In some cases ways may need to be found to provide additional financial support (i.e. subsidies or cross subsidies) for services to remote locations to ensure a minimum level of accessibility and mobility for the most disadvantaged communities.

6.1.2. Poor Quality Infrastructure

Although this is often not the obstacle it is commonly perceived to be it can be an important disincentive to operators. It is recommended that providing basic year round vehicle access is a minimum requirement and this is best achieved through a policy of spot improvements.

6.1.3. Poor Diversity of Vehicle Types

The diversity of vehicle types in SSA is much lower than in many Asia countries. Diversity is important for meeting all transport needs and ensuring a competitive environment. The most important categories are bicycles, animal transport, tractor technology, pickup, trucks and buses. Extension advice, demonstration projects and the availability of credit on reasonable terms could be very helpful in extending the range of vehicle types. For some countries unconventional (but very effective) vehicle types –such as the converted power tiller- are prevented by law from operating as a transport vehicle (Ellis 1996).

6.1.4. Uncompetitive Transport Markets

Although rural transport services have been predominantly supplied by the private sector in much of SSA and government control has been reduced, the current institutional structure has lead to uncompetitive practices. Transport unions, associations and informal cartels have often taken the place of governments in setting fares, licensing routes and rationing the supply of vehicle services through queuing at bus and truck parks (see Fouracre et al, 1994). In many countries strong unions significantly distort transport markets keeping charges high and utilisation low. Various measures will have to be undertaken to control the actions of cartels including an explanation of the issues, consequences and potential benefits. Local Authorities and user groups also need to be brought into the dialogue to ensure that there is some countervailing power to the union activities.

6.1.5. Lack of Understanding

There is a lack of understanding by government, donors and other agencies of the potential benefits of increasing the efficiency with which transport services are provided. A number of studies have shown that rural and interurban transport costs in Africa range between two to six times the corresponding costs of transport services in many Asia countries. The reasons for these differences in costs relate to higher input prices for vehicles and parts, Uncompetitive transport practises reducing vehicle utilisation and high maintenance costs most often related to poor vehicle maintenance procedures. The implications of substantially reducing transport costs for increased demand for travel, lower food and commodity prices and increased incentives for agricultural production could be very important. The potential benefits could be worth many billions of dollars to many SSA countries (Hine and Rizet 1991).

6.1.6. Transport as a Basic Need

John Howe (1996) has argued that transport is a basic need (in the same way that water or shelter is a basic need) and that people have a right to mobility. For their own internal purposes many developed countries recognise that transport is a basic need and when necessary subsidies are provided for those that are strongly disadvantaged. Rural transport services are subsidised in the UK and in many countries. Over the past three decades aid agencies have been keen to support rural road infrastructure but there has been a belief that the market can be safely left to look *after* transport services. However as is pointed out above because of the nature of the situation a market failure has occurred and adequate transport services have often not materialised. Because of the low service frequency, poor roads and high costs of travel the remote rural populations of Africa suffer the greatest disadvantage in terms of access to useable transport services. There are many examples of communities living along roads with traffic levels as low as a few vehicles per week or month and even these vehicles are not primarily for the use of the local population. If people want transport they may have to walk ten kilometres along the road to a junction where they will have a better chance of getting transport.

Without access to regular transport services the possibility of engaging in economic activity beyond the immediate realm of the local village or gaining access to more than the most elementary health care or education will inevitably be severely constrained.

6.2. A Possible PPP Project

As part of a PPP project to improve the provision of rural transport services a wide range measures will have to be taken in order to ensure the project is successful. It is likely consideration will have to be given to the following:

- Controlling transport cartels, reducing tariffs and increasing service frequency
- Reducing import prices of vehicles and parts
- Devising training programmes to indicate the advantages of slow and careful driving and the importance of routine maintenance
- Consider ways that surplus capacity of old vehicles may be removed from the market
- Devising methods to financially support a minimum of frequency of transport services that cannot be supported through other means.

In order to gain the maximum co-operation of transport operators it is proposed that a package of measures are discussed and negotiated in detail with the operators and the measures implemented at the same time. In this way the operators can see that by changing their behaviour they can be brought into a "win-win" situation.

6.2.1. Market Failure

It is important to recognise that the provision of transport services in many developing countries has been poor because of market failure. High transport charges occur because the Uncompetitive environment sustains a combination of high vehicle and parts prices, low vehicle utilisation and high maintenance costs. The low vehicle utilisation is a function of many high cost operators being kept in business by the way that the transport cartels control the lorry parks with vehicles sometimes waiting in a queue for days or weeks at a time for a load.

With transport cartels operated through rationing of demand at the truck parks an excess of supply leads to an increase in transport tariffs. In a purely competitive market an excess of supply would lower tariffs. A clear example of how an excess of supply can raise transport charges, where supply is rationed through queuing, comes from Nepal. When new roads were introduced in mountainous areas the demand for commercial portering services fell as demand switched to motor vehicles. As a result the remaining transport routes, which were not subject to road competition, now had more porters than before looking for work. The consequence was that portering tariffs rose substantially to help ensure that the remaining porters continued to have a living wage because they each now had less work to do. The porters refused to work for less and there was no alternative competition because of the way they queued for work (see Blaikie et. al. 1976).

Most developing countries do not have active policies against monopoly and cartels. Direct price control is perhaps the main and often only weapon used by governments in this area. Annex 4 provides a brief review of cartel policy in the EU, UK and USA.

6.2.2. Vehicle Utilisation and Surplus Capacity

Vehicle utilisation could be increased by a combination of policies. The surplus vehicle stock encourages inefficiency through the sharing out of demand via the queuing system. Surplus capacity could be reduced by a policy of buying out and scrapping the older vehicles. A more rigorous enforcement of vehicle inspections could also help to remove the more unsafe and polluting vehicles. The number of truck and bus parks could be increased. This would automatically increase the number of vehicles "available for hire" and reduce collusion on prices.

Reducing surplus capacity by buying out older vehicles is obviously a controversial measure. There is an obvious problem in that, without scrapping, the purchased vehicles would return to the cartel operation as before. There is no direct way of knowing, a priori, whether the policy would be effective. It is put forward as a possible way of giving some short term inducement to remaining operators to co-operate with the project and help them increase their utilisation. The current demand may then be spread among fewer operators and overall costs could be reduced.

It has been recognised for some time that overmanning and surplus capacity can hinder efficiency. In recent years the World Bank has given some support to reduce overmanning in the public sector of many developing countries. The issue of downsizing and retrenchment is considered in Annex 5. The European Common Fishery Policy provides an example of buying out capacity and this is reviewed in Annex 6.

6.2.3. Service Availability and Route Licensing

One way of increasing the availability of transport and increasing competition in the market place would be to encourage and establish the use of new vehicle types. Bicycle, rickshaw and motorcycle stations are common in both urban and rural areas of many Asian countries for the shorter distance movements. Agricultural tractors and trailers, power tillers adapted for transport purposes or motorcycles with side cars could all be used to carry heavier loads on relatively long routes that have a lower density of demand. New forms of transport operating from different terminals could be very useful in establishing a new dimension of competition. Different vehicle types have different characteristics and would require different fare structures.

To increase service frequency and provide services to the remoter locations on social grounds the routes could be licensed and operators could be required to run services to a timetable. This would often mean leaving the bus terminus before the vehicle is full.

If this happened there would be greater chance of passengers being able to board transport someway along the length of the route. As is mentioned above for many of the more remote rural routes there would be a need to subsidise or cross-subsidise the operation to provide a minimum service on social grounds. This is very common for high income countries.

The government control (or authorisation) of fare and truck tariff levels can play some part in helping to keep down prices. However this does need to be treated carefully; posted fare levels have also been used as a way to collectively prevent operators from accepting lower fares levels.

Lower fares and tariffs and greater trip frequency would help to encourage an expansion of the market. If rural communities were more certain of a regular service then they would in time plan their affairs (in terms of crop marketing, job seeking etc) to take advantage of the new situation.

One solution for thin transport passenger markets is to licence a number of routes together and require operators to competitively "bid for the market". Route frequencies, fare levels and the amount of any required subsidy would be made explicit in the bidding and negotiating process. Groups of existing operators could be encouraged to form companies to place bids. Bidding for routes is used in high income countries and may be appropriate for certain operations in Sub Saharan Africa.

One drawback of the approach is that once the bid is accepted and the service in place further competition may be curtailed. Furthermore bidding "for the market" implies an element of cross subsidisation between routes. In order to guarantee that the operator will run on the routes with low demand there may be a requirement for some protection from competition on the profitable high demand routes. In rural locations this may be difficult to enforce.

6.2.4. Possible Methods of Subsidising Rural Transport Services

Within developing countries most transport subsidies have not been explicitly aimed at the rural poor. In some countries fuel prices and bus fares have been held down. These have largely been designed to protect (the richer) urban population from price inflation. Because rural transport is more informal, and is very largely supplied by the private sector, rural transport operators have not received direct operating subsidies to the same extent as their urban counterparts.

In high income countries a variety of transport subsidies have been employed. In the past the UK government has employed fuel subsidies for buses and bus grants (provided on rural travel distance basis) for rural routes. Specific route subsidies have been provided by the Local Authorities. A review of the effects of bus deregulation and route subsidies is included in Annex 3. The implications of using "net" or "gross" cost subsidies are examined in Section 3.5.

It has been argued that subsidising services does not always reach those people most in need of help with transport costs. The major beneficiaries are usually the richer sections of the population that travel most. Methods of directly targetting specific groups are travel passes and travel token schemes which can be adjusted to suit local conditions. For example travel passes can be issued to allow for free fare, half fare etc and like tokens they can be distributed according to specified criteria. Like all subsidies schemes tokens and passes may be subject to abuse. For example, the most likely abuse is that the token will be sold on to others and not be used for those it was intended. Even if this happens the original recipients will be major beneficiaries of the schemes.

Travel tokens and passes have long been used in the UK to aid the mobility of the elderly with schemes varying from county to county. Results of some schemes are reported in Balcombe, Astrop and Hill (1998).

In the current environment it is unlikely that subsidies will play a large universal role in a new PPP arrangement however they should be examined carefully particularly as a solution to providing transport to the most remote locations where there may be no regular transport service provided. Or where service frequency is measured in weeks or months.

6.2.5. Vehicle Prices

It has long been recognised that substantial price differences for the same product can persist for long periods in different national markets. However exchange rates and differences in taxation can disguise the differences to some extent. Differences in vehicle prices in different markets are not uniquely confined to Africa and Asia. Car prices in the UK have been higher than in the rest of Europe for over two decades. Recent press publicity has indicated that for certain models prices might be 60 per higher in the UK than in the cheapest European market. Although there has been some reluctance to tackle this problem (perhaps because of the implications for manufacturing employment) there are recent indications that steps may now be taken to introduce more competition and restrict the monopoly power of exclusive dealerships.

The evidence from a number of studies suggests that new (without tax) prices of imported trucks are commonly two to three times the price in Africa compared with Asia. By concerted bulk buying policies (by government, aid agencies, or larger commercial firms) the prices of new vehicles could be substantially reduced. Exclusive dealerships (dealing with relatively small numbers) also make the prices of spare parts very expensive (Rizet and Hine 1993, Hine et al 1997).

6.2.6. Vehicle Maintenance Costs

Very substantial differences have been found in vehicle maintenance costs between Africa and Asia. Although some of the differences may relate to differences in road surface roughness it appears that driver care, low driving speeds and attention to routine maintenance (particularly changing engine oil frequently) are of critical importance. Training programmes would be extremely cost effective if a few simple messages on the issues could be got across to owners and drivers.

6.2.7. Other Constraints

The introduction of the types of measures highlighted above would need to be supported by a series of other activities tackling other constraints to improved rural transport services. For example a package of demand management which tackles access to markets and market information; the establishment of transport brokering companies to match empty vehicles with loads; the use of modern communications to "order" transport services and transfer information; and network planning measures to maximise the interconnectivity of routes and to ensure that returns from limited budgets are maximised through the use of spot improvements to maintain passability on as much of the network as possible. Rural credit may also need to be considered if IMT's are to be successfully introduced. Training programmes are also required on a wide range of topics such as vehicle maintenance and management. Many of these activities will require close co-operation with non-transport organisations.

6.2.8. A Possible Programme

In order to ensure the highest possible level of success in bringing about a major change in the provision of rural transport services it is essential to achieve the maximum degree of co-operation by transport operators and other interested parties. To achieve this it is suggested the following steps are taken:

1. Senior political leaders and government officials must be made aware of the issues and the very large potential benefits. It is important to remember that a significant improvement in rural transport services would have an effect on the economy of many times that of improvement in road maintenance standards.
2. Political leaders should then be asked to show a commitment to the changes by "signing up" to the process. This could be part of a revamped form of the Rural Travel and Transport Program (RTTP) which is part of the Sub-Saharan African Transport Program (SSATP).
3. External donors should be identified and asked to commit funds and also to "sign up" to the change process. Donor money should be made available to help implement the new policy and pay for the following costs: the administration, surveying and the planning of the pilot project, the training of operators and drivers, the buying out of surplus capacity, the initial financing costs of arranging the import of cheaper vehicles and parts, subsidies for remote transport services for an initial period of running the pilot project.
4. Local 'champions' of the change process must be identified and briefed. These might be politicians representing rural areas, representative of user groups, senior civil servants etc.
5. Budgetary arrangements should be set up to pay for the administration costs and other costs of the programme. A new governmental cell should be set and officials selected to plan, and monitor changes.
6. Pilot areas should be identified in which the new rural transport policy can be tried out.
7. Surveys should be organised to collect data on the current rural transport patterns, fares, vehicle prices etc of regions initially identified to pilot the changes.
8. The survey data should be analysed to identify existing frequencies of passenger, vehicle and load movements for different routes. Typical revenue and cost profiles should be prepared for different vehicle types.

9. Alternative solution plans should be prepared for each pilot area. Possible solutions might involve the introduction of new competition via new transport operators and modes (e.g. new NMTs or IMTs) or the introduction of route licencing involving contracts to undertake new forms of operation. The plans may include driver and operator training, operating subsidies for routes to the most remote communities and the buying out of capacity where it is obvious that cartels are sustained through the gross oversupply of vehicles.
10. Press and media publicity must be organised to inform the public of what changes might take place.
11. Necessary changes in transport legislation must be organised and passed.
12. Exhaustive discussions must be held with operators, politicians, local authorities, user groups and transport operators.
13. Assistance and possibly finance should be made available to a new or an existing vehicle importer to establish contact to import cheaper vehicles and vehicle parts, (most probably) from Asian suppliers. Any vehicle and use regulations preventing the supply of cheaper vehicles should be identified, investigated and dealt with.
14. The area pilot plans should be modified to take account of the views of interested parties.
15. Transport operators should be persuaded that if they give up their current restrictive practises, accept lower fares and increase their trip frequencies under new route licensing contracts then they will get the following benefits:
    a) lower new vehicle and parts prices
    b) training on how to run and maintain their vehicles more cheaply
    c) a proportion of their capacity (of older and obsolete vehicles) will be bought out and scrapped.
    d) subsidies for operating of the least traffic and most remote routes.

16. The above activities should be put into the context of sustainable rural livelihoods through the examination of existing household constraints, rural-urban linkages and cross-sectoral linkages.

7. A LOG FRAME

Proposed project logframe for Public Private Partnerships project

Narrative Summary	OVIs	MoV	Assumptions
Goal: 1. Sustainable improvements in rural livelihoods.	1.1 Increased economic and social activity.	1.1 Consultants' impact monitoring	(goal to Supergoal)
Purpose: 1. Sustainable reductions in the cost, and increased service frequency and service reliability of rural transport services resulting in improved access for rural households.	1.1 20% reduction in goods and passenger fares in countries where reform has been adopted by 2005. 1.2 20% increase in trips made by rural households and business by motorised and non-motorisd transport by 2005. 1.3 20% increase in attendance at schools, clinics and markets by previously disadvantaged residents/ farmers by 2005.	1.1 Transport surveys 1.2 Household surveys 1.3 Household and business surveys	(Purpose to Goal) 1. That improvements in livelihoods can be translated in to opportunities to increase economic and social activities.
Outputs: 1. Sustainable reform process in at least two countries in the transport sector which includes politicians, private operators, unions/ associations, farmers groups, user groups and donors. The reform process will be complemented through a number of initiatives as set out below in outputs 2-6.	1.1 Extensive consultative exercises undertaken by end 2000. 1.2 Framework for reform process and operating format agreed by 2001. The basis for a Public/Private partnership agreed upon. 1.3 Host organisation for reform process identified. 1.4 Private operators identified to participate in some or all of the project outputs as set out in this logframe by 2002. 1.5 Quarterly steering meetings held in participating nations by 2002. 1.6 Policy reform measures passed by parliament by 2001.	1.1 Consultants reports. 1.2 Policy document. 1.3 Legal framework of host organisation. 1.4 Consultants reports. 1.5 Minutes of steering meetings. 1.6 New laws passed in parliament.	(Output to Purpose) 1. The reform process is successful in meeting its objectives. 2. The supporting activities to the reform process are practical to implement and have the desired effect. 3. That recommendations arising from steering meetings and research are implemented as part of the reform process.

Narrative Summary	OVIs	MoV	Assumptions
2. Institutional reform of the transport industry and removal of institutional constraints to improved transport services.	2.1 Measures to reduce restrictive practise in the transport industry by 2001. 2.2 Measurable increase in competition between operators. 2.3 Training programme for mechanics, drivers and operators to be underway by 2001. 2.4 Method produced to financially support operations in low demand areas by 2001.	2.1 Consultants reports. 2.2 Consultants reports. 2.3 Training courses. 2.4 Consultants reports.	
2. An increase in vehicle choice, availability of services and efficiency of existing vehicle fleet.	3.1 Excess fleet capacity bought out by 2002. 3.2 3 New vehicle types (power tiller, E-tan and motorcycle tech.) introduced by 2002. 3.3 Private company formed to source spares from other countries or regions by 2002. 3.4 At least two cost incentives provided by government to rural operators by 2002. 3.5 Research undertaken to determine demand implications of operating vehicles at pre-determined frequencies and fare levels.	3.1 Consultants reports. 3.2Consultants reports. 3.3 Legal framework for company. 3.4Consultants reports. 3.5 Research report.	
3. A programme of demand management to artificially increase the density of demand in rural areas.	4.1 Area targeted for increasing the number of markets - whether fixed or mobile. Average distance to market reduced to 15kms by 2002. 4.2 Area targeted for increasing the interconnectivity of routes. Dead-end routes on rural roads reduced to 20% of total network by 2002. 4.3 Project set up to demonstrate advantages of transport brokers and communications technology in matching empty vehicles with loads by 2002.	4.1 Consultants reports. 4.2Consultants reports. 4.3Consultants reports.	

Narrative Summary	OVIs	MoV	Assumptions
5. Implementation programme of appropriate infrastructure solutions and prioritisation methods	5.1 200kms in target area rehabilitated/maintained using spot improvement techniques by 2001.	5.1 Consultants reports.	
	5.2 Agreed procedures for the prioritisation of expenditure, both between public and private sector and between competing roads and the appropriate engineering interventions.	5.2 Research reports or set of guidelines.	
6. Cross programme and research issues disseminated and published.	6.1 Environmental, social and gender issues identified and managed by 2001.	6.1 Consultants reports.	
	6.2 Research on impact of reform process on rural livelihoods and the development process by 2005.	6.2Research reports.	
	6.3 Research identifying impact of outputs on price, availability and demand for transport by 2005.	6.3Research reports.	
	6.4 Toolkit produced based on demonstration projects providing other countries with model for appraisal and best case scenarios by 2005.	6.4Guidelines or manual.	
	6.5 Quarterly international steering meetings held to disseminate experience and agree policy and strategy by 2001.	6.5 Minutes of steering meetings.	
Activities: 1.1 Increase awareness of political leaders, government officials and donors of benefits. 1.2 Political leaders to "sign up" to reform process. 1.3 Donors to "sign up" and commit funds to the process. 1.4 Local champions to be identified and empowered. 1.5 Discussions with private companies to identify areas of mutual interest. 1.6 Organise steering meetings. 2.1 Produce a package of reform measures and work towards implementation.			1. Ability to persuade politicians of benefits and Political will to start a reform process. 2. Ability to persuade the other stakeholders that reform is worthwhile and beneficial. 3. Private companies can be found who are willing to participate in process. 4. Donor/ government funds available. 5. That local and international champions can be found to take the process forward.

Narrative Summary	OVIs	MoV	Assumptions
2.2 Organise a national training programme for operators and mechanics.			
2.3 Produce plan for the support of services in low demand areas.			
3.1 Identify appropriate vehicles for introduction.			
3.2 Establish a company to source spares and vehicles.			
3.3 Lobby government to provide tax incentives to rural operators.			
3.4 Operate new vehicles with fixed frequency and fare levels to determine real demand.			
4.1 In conjunction with Ministry of agriculture increase the number of markets.			
4.2 Identify key infrastructure links and construct/ rehabilitate to produce interconnectivity.			
4.3 Establish companies to act as transport brokers.			
4.4 Provide funds and expertise to examine possibilities for using communications technology.			
5.1 Identify and use spot improvement techniques on target roads.			
5.2 Use existing work, and new research where necessary, to develop prioritisation criteria. Social and economic criteria should be used.			
6.1 Identify programmes of research to track and monitor success/failure of reform process.			
6.2 Organise steering meetings, seminars, papers and other means of disseminating research.			
6.3 Produce "toolkit" to help appraisal process and to foster best practise.			

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ANNEX 1 REVIEW OF BACKGROUND LITERATURE

A1.1 Augenblick, M & Custer Jnr. (1990), "The Build, Operate, and Transfer ("BOT") Approach to Infrastructure Projects in Developing Countries". World Bank Working Papers (WPS 498), Washington DC

This report examines the characteristics of BOT projects, host government support, risk allocation, the necessary conditions for feasible BOT projects, cost and procurement issues, arguments for and against BOT projects, and World Bank involvement to date, as well as future assistance to host governments. The key considerations are detailed as being:

- Legal environment
- Economic environment
- Host country credit rating
- Political environment
- Sector characteristics
- Cyclical considerations

The author believes that BOT infrastructure projects are by no means the perfect solution for developing countries, as they tend to be exceedingly complex from both a financial and legal point of view. The time period they need to develop and be negotiated is also seen as a potential difficulty.

The author does acknowledge however that BOT is a real option in countries not able to finance all of its infrastructure needs on the basis of budgetary resources or sovereign borrowings. He foresees that as BOT methods and operations become more widely accepted (as hopefully will standard solutions to the various issues that are posed) projects should become somewhat easier to negotiate and implement. Sponsor commitment of equity (a feature of BOT) ensures they will also remain committed to the projects successful operation over the concession period, which is an added bonus of such projects.

The author finally highlights to host governments the importance of recognising and accepting the complexity and time consuming nature of the process, the extensive host government support which will have to be provided, and the rates of return which commercial lenders and private sector equity investors will expect.

As long as this is understood, says the author, the BOT approach appears to be a useful possible alternative to the conventional financing and operation of infrastructure projects in developing countries.

A1.2 Beilok & Stanchev (1997), "Road Transport in the Balkans". Transportation Quarterly - Fall 1997 Volume 51, Number 4, USA.

The article explores factors that contribute to slow, high cost transport along roadways in Bulgaria, Macedonia FYR, and Romania. The primary focus was the identification of factors not related to the infrastructure, with interviews revealing concerns over security, the clarity and fairness of laws and regulations, and the competency and honesty of officials (these interviews were with international motor carriers). The average respondent indicated that when travelling through Romania, 74% and 79% of the time respectively, officials solicit bribes from truck drivers, and many reported long delays at border crossings. This raises questions regarding the efficacy of costly projects to expand the infrastructure. In capital-poor societies with enormous needs for investments in virtually all areas of their public and private sectors, the opportunity costs of using scarce investment funds are exceedingly high, so it is crucial to avoid unnecessary or premature investments.

Example: Bulgaria/Romania Border-Crossing at Russe
A primary crossing and the site of the only bridge across the Danube between the two countries. Even with the observed low volume of traffic, vehicles took several hours to pass through the border. Along with the recognition of the need to expedite international movements of freight and passengers, the governments in question have pledged to build at least one and possibly tow new bridges. The cost is estimated at $500 million per bridge - around 1% of their combined GDPs - (equivalent to the US committing to an $80 billion infrastructure project). Research results strongly suggest that the delays at Russe are more to do with cumbersome procedures and inept, negligent, or corrupt applications of those procedures and nothing to do with insufficient road capacity. Even with a new bridge, the situation would change little without changes to the legislative/administrative system and procedure.

Introducing changes to alleviate these problems would be politically and bureaucratically difficult, but could result in significant expansions in the capacity of the transport system for a small fraction of the cost of building new infrastructure, e.g. the huge increase in Mexico/US crossings over the past 10 years largely through the streamlining of procedure. A report at this border suggested that congestion, when it occurs and despite the significant increases in traffic, is due to delays in processing rather than the physical infrastructure.

The report thus concludes that the results of the Mexico study suggest that the depressed volumes of freight throughout much of the region and the widely recognised prevalence of problems among border officials and internal police, priority should be placed on reforms rather than construction. Whilst most policy-makers in the region would probably agree with this argument, the chances of them instituting and maintaining such reform is slight, says the author.

A1.3 Bennathan, E & Thompson, L (1992), "Privatisation Problems at Industry Levels – Road Haulage in Central Europe". World Bank Discussion Paper No.182, Washington DC

The report examines the problems and processes of privatisation in the so-called 'transitional' economy. The main problems seem to relate to strategy and precedence, in that it had not previously been attempted with an economy that had been centrally planned. A major theme of contention is the speed of privatisation, weighing up priority accorded to political and equity objectives over those of economic efficiency.

It is noted that the depressed nature of such economies often accounts for excess capacity in road haulage, although they often compare favourably with market economies in terms of organisation, enterprise sizes, and diversity of operations.

Problems at management level were identified as 'gaps of knowledge', where managers were often skilled in many areas but lacked completely in others, potentially making road haulage industries less viable under competitive conditions.

The principle of *caveat emptor* does not apply reliably in transactions between state and private parties capable of summoning political support, and thus casts doubt over the transferral of enterprises of doubtful viability. Recommended strategy is that the more viable enterprise be transferred first, with assisted programmes of commercialisation for the remainder following later.

Leaving firms to 'get on with it' is shown not to induce the necessary change, with state intervention being deemed necessary to begin with. This, in turn, requires explicit mechanisms. On the other hand, staged reform requires a programme and an institution to implement it, with legal frameworks often the difference between success and failure.

The changes implemented in the said economies have left transport industries virtually free of regulation, but the report points out that in the market situation, it will be necessary for the government to fashion instruments of economic control, which in turn may have implications on the freedom of the sector.

The report also highlights the need to 'separate freight from transport', with establishments (not just accounts) needing to be separated. Prejudice appears to have become commonplace due to past abuses and suspicion of political compromise among enterprise bosses. Enterprises should therefore be held accountable to an institution capable of exercising ultimate control.

A1.4 *Carbajo, J (1993),* **"Regulatory Reform in Transport – Some Recent Experiences".** ***World Bank Synopsium, Washington DC***

The theme here is that government intervention often arises because of what the author calls 'functional failure' of markets – i.e. that in some cases the market can fail to provide certain services efficiently and effectively. Reasons given for the said failures are:

- Imperfect information among market agents;
- Presence of externalities;
- Imperfect competition;
- Existence of increasing returns to scale.

The resulting government intervention can be either direct (legislation and administrative regulation of prices, quality of service, entry/exit from the market), or it can be indirect (anti-trust regulation intended to control firms in the unfettered exercise of their market power).

It is noted that in the past, transport service and the myriad of government intervention/control, as he puts it, has gone well past regulation that has health and safety as its primary motive, with examples including rate regulation (railways), entry restrictions (trucking), minimum levels of service (urban buses), and cargo reservation (shipping).

The author believes that regulation should ultimately improve the allocation of resources.

A1.5 Edmonds, G (1998), *"Wasted Time: the Price of Poor Access"* RATP3 Ch.8, ILO Policies Development Unit, London

This looks at planning for the public and private sector. In developing countries the focus has been more on the improvement of access, as opposed to market and performance in industrialised countries. The common challenge here is seen to be how to deal with non-public-sector investment and the market system, and that road infrastructure will be predicated on economic analysis and should therefore respond to the potential of the area.

The article asks if only the market should regulate transport services, or if it should be treated as a public service which encourages development. The author believes that Accessibility Planning can identify the need for a market centre, but it will often be the case that the private sector will be required to invest in such a facility.

The answer postulated is that it depends on each governments approach to public-sector provision. In the centrally planned system of Lao Pd for example, the government may feel it to be a responsibility to stimulate economic development by means of directly providing such services. In the Philippines, says the author, the government is more likely to feel that these should come from private initiatives.

A1.6 *Farcas, Z,* "Public and Private Co-operation in the Provision of National Forest Roads" (US)

Although this relates to forest roads in a developed country, the author feels that policy conclusions and requirements may be applicable to rural road systems in other regions of the world. The article charts trends in the planning, funding, management and maintenance of forest roads.

It states that the co-operative provision of national forest roads has long been established in the US, with plans containing the programme for private sector development and public use of the forest resources. The Forest Service relies heavily on the private involvement and co-operation for finance and resource development.

Private sector involvement with maintenance is stressed, as it is with construction and reconstruction. Institutional and legal constraints to more public-private co-operation in the provision of roads exists in the US as well as other countries, and the author requires that this has to be lessened for greater co-operation in rural areas.

He concludes with the thought that for the public and the private sectors to properly manage and use rural resources, road systems must provide a high degree of accessibility to those resources. Road systems will be more likely responsive to the dynamics of economic activities when public-private co-operation in their provision occurs.

A1.7 Galal & Shirley (1994), *"Does Privatisation Deliver?"* Economic Development Institute of the World Bank, Washington DC

Winners and Losers in Privatisation

(Leroy Jones)

The author feels the main fear from the standpoint of the *consumer* lies in monopolistic/oligopolistic exploitation, and that divestiture may lead not only to more efficient operation, but also to more efficient exploitation of consumers.

The question is if the loss to consumers is (as in Mexico - primarily because of higher prices) an indication of a failure of divestiture? The author believes it is not because loss derived from price increases reflects a shift from high subsidies to economically rational pricing. So although the rise in prices from uneconomically low levels hurt consumers initially, in most cases this loss was offset quickly by increased investment and expansion that reduced waiting time and rationing.

Not a single case was found by the author to have made *workers* worse off, even for those who lost jobs (taking into account their severance pay, expected time out of work, and expected earnings when they go back to work), as workers generally have some power to negotiate a favourable deal during privatisation.

The conclusion was that the patterns of the effects shown by the author indicate that divestiture has clearly been a successful policy, if not a perfect one.

Relatively few generalisations can be made about divestitures, for a simple reason. Divestiture is a move toward control by market forces, a push toward more efficient mechanisms. But the direction of that push depends on the starting point and the distortions in the economy. These distortions have been quite different, and so the pressures imposed by markets have been quite different. Although the net impact of market forces has been positive, the nature of the impact depends on the circumstances.

For this reason the author guards against using the results of the study to predict results elsewhere; even in countries similar to the sample. Type of country, in terms of economic ranking, will also render different results.

Prediction is not recommended, although the results can be used for what the author describes as prescription, in order to talk about what divestiture requires. A successful divestiture is not a single policy decision, but an integrated package of a large number of individual decisions.

A1.8 Heggie, I (1991), "Improving Management & Charging Policies for Roads: An Agenda for Reform". *World Bank Report INU 92, Washington DC*

In the context of its title, the report examines the characteristics of roads, policies towards roads and the problems with such policies, the importance of improving the management of roads, as well as the need for improving charging policies for roads.

The report states that the replacement costs of main roads in developing countries approaches $300 billion, but that with the introduction of commercial cost-accounting systems, this cost can be reduced by between 5-15%, while sub-contracting for road maintenance can be shown to reduce them by a further 20%.

Given this, and the generally accepted notion that public agencies tend to operate 'better' when faced with an element/form of competition, Bank policy has been to *commercialise* or *corporatise* public-sector agencies. This ensures market discipline, hard budgets, clear objectives, and sufficient managerial autonomy.

Work is not just at the firms level, but also at sector level (albeit more limited) by concentrating or increasing allocations for road maintenance, reducing force-account work, sub-contracting work to the private sector and other government agencies, and strengthening management information systems. The author notes that little attempt has been made to improve the overall operation and management of roads.

Externalities must, say the author, be considered with everything. But the main focus is on charging and on the management of roads. To improve the situation, Heggie recommends making the performance of the road agency more transparent, linking revenues to expenditures. The strengthening of institutional arrangements for road management and the setting of clear objectives (and monitoring performance against these objectives) should also be considered.

In terms of charging policies, the author believes that an informed user (by way of clear pricing) is an effective method of market discipline and of discouraging monopolistic behaviour. Heggie notes that user charges should never be set lower than variable costs (road maintenance costs, public costs of road accidents, and a contingency fund to cover the costs of uninsured road accidents).

A1.9 Heggie, I & Vickers P (1998), *"Commercial Management and Financing of Roads"*. World Bank Technical Paper No. 409, Washington DC

The report reviews the state of the road sectors in developing countries, the importance of roads and road transport, the impact of poor maintenance, past efforts to reform, and regional programmes. It examines what the authors believe to be the causation of the problems, namely weak institutional frameworks and weak management, weak works and poor financing facilities.

Issues surrounding the 'commercialisation' of roads are seen, in turn, to involve assigning responsibility, creating ownership, ensuring secure and stable financing, sound business practice, and an agenda for reform.

It is indicated that responsibility must be assigned, and it could be to either central or local government, a community group, or a private entity. The development of commercially oriented agencies to administer etc is encouraged since they promote managerial responsibility.

In terms of creating ownership, the author believes it will create a 'surrogate market discipline'. The challenge, they believe, is to identify an appropriate institutional mechanism that can effectively involve politicians and road users in the objective, depoliticized discussions about road management.

In the reports field of interest, roads, the setting up of a road board, and the issues surrounding it, are discussed. It is imperative to decide if the board should have executive powers (which will require new legislation) or if it should simply operate in an advisory capacity. Board members should ideally represent constituencies that have strong vested interests in well-managed roads. The board should have clear terms of reference in order to (among other things) spell out the relationship between the board and the parent ministry.

Regarding ensuring an adequate and stable flow of funds, the report believes the idea should be to set clear market signals (licence fees, fuel levies, international transit fees, and tolls) and to have sensible pricing and recovery policies. This will improve domestic revenue mobilisation and reduce the welfare costs of taxation, and lower general consumption taxes. To maximise net economic benefits, road user charges should be set equal to the costs of the resources consumed when using the road network.

A1.10 Kerf, M & Smith, W (1996), "Privatising Africa's Infrastructure". World Bank Technical Paper No. 337, Washington DC

The report identifies 'private participation options', amongst which there are management contracts, concessions, leases, de-monopolisation and divestiture. Four main challenges are identified in realising the potential of infrastructure privatisation: low per capita income and low economic growth (making Africa 'less attractive' for investment, the affordability of cost-covering tariffs are seen to be over-emphasised, and the long-standing culture of debt default.

The report also considers other areas that the author feels need to be addressed in order for progress to be made. They include the establishment of adequate legal and regulatory frameworks, methods for dealing with non-commercial risks, and the mobilising of local finance.

Strategy recommendations for entities such as the World Bank are then given, such as involving all parties in dialogue, cross-sectoral issues and options assessments, and taking into account past experience.

Main Forms and Potential Benefits of Infrastructure Privatisation

	Management Contract	Lease	Concession/ BOOT	De-monopolise/ BOO	Divestiture
Management Expertise	♦	♦	♦	♦	♦
Tariff Discipline		♦	♦	♦	♦
Access to Private Capital			♦	♦	♦
Capital Market Development			♦	♦	♦
Potential Capital Revenues					♦

The report gives examples of projects for each of the above classes. Management contracts, Guinea-Bissau Electricity Sector; Lease, Ivory Coast Water Supply and Guinea's lease for Water Supply; Concession/BOOT, Cameroon Airport Concession; De-monopolise/BOO, Ivory Coast Independent Power Project and Cellular Telephony in Ghana; Divestiture, Sub-Saharan Africa generally.

The authors seem to indicate that negligible commitment to commercial principles is the major source of public failure. It then goes on to discuss, given the ultimate objective of securing private investment, the main benefits associated with privatisation and the different forms that this can take.

Concern is also expressed over how to deal with risk and changes to legal and regulatory frameworks. Local finance availability is another important aspect, both in terms of foreign and local sources.

The author believes that foreign financing is limited by convertibility, transfer, and exchange rate risks, and also by political acceptability and government commitment. The authors also comment on what they believe is required to successfully mobilise local capital for private infrastructure projects in Africa. Critical elements include reduced political uncertainty, fiscal discipline, more efficient financial discipline, and better information.

The publication also details elements linked to the different sources of local financing in Sub-Saharan Africa. Internal cash generation is often an important source, and also low equity may be sourced from publicly traded stock markets or from private sources such as venture capital. There is also consideration given to the rapidly developing stock markets in Africa – see table below.

Stock Markets in Sub-Saharan Africa 1992-1994				
Market	**1992 Mkt Cap millions US$**	**1992 turnover millions US$**	**1994 Mkt Cap millions US$**	**1994 turnover millions US$**
Botswana	295	15	377	31
Ivory Coast	336	4	428	12
Ghana	84	0	1 873	75
Kenya	607	12	3 081	62
Mauritius	416	10	1 514	85
Namibia	326	0	9 574	18
Nigeria	1 221	14	2 711	18
South Africa	103 537	7 767	225 718	15 954
Swaziland	111	0	338	1762
Zimbabwe	628	20	1 828	176
Total	**107 561**	**7 842**	**247 442**	**16433**

They identify that this element needs further development if more substantial foreign investment is to be attracted, so reforms and restrictions will need to be addressed. They also note that the development of these markets will be linked to the development of the private sector. In addition, as stock markets develop, the number and variety of local participants increase. They note that several African markets are seeing the emergence of local mutual funds, which mobilise funds from retail investors for investment on the stock market.

Other issues they are concerned with attracting private equity funds, promoting the establishment of private pension funds and other institutional investors, and mobilising local debt.

A1.11 Lockwood, S (1997), *"Public Private Partnerships are the Answer: What is the Question?"* Transportation Finance for the 21st Century - Proceedings of a Conference - Dallas, Texas April 23-25 1997 Transportation Research Board, USA

"...change in roles and relationships based on a new mix of complementary public and private resources (expertise, technology, finance) pooled toward a common objective - while still achieving the partners' respective separate objectives."

The author believes that finance and institutional roles are inextricably linked. New sources of revenue and financing methods have resulted in a new configuration of sectoral roles, and the related formal reallocation of risks and rewards constitute "Public Private Partnerships".

Experiments by States in the US during the 1980s were generated by project-specific requirements, especially in areas with high needs that traditional finance and delivery methods could not supply. In the early 1990s, federal, state, and local government transportation programmes continued to be constrained by a combination of what is termed the "four D's", shrinking their financial capacity:

- deficits
- downsizing
- devolution
- deregulation

It is identified that over time, legislation and regulation have begun to specifically encourage the commingling of toll and other public and private resources in cost-sharing arrangements with private road development entities. In addition it has permitted new forms of project delivery such as *Turnkey* development, and established new frameworks for programme finance such as state infrastructure banks.

Key Milestones in Federal Legislative History

LEGISLATION	*KEY FEATURES*
ISTEA (1991)	• Allows conversion of free federal aid roads (non-interstate) to toll roads for reconstruction • Permits the commingling of federal aid with toll-based revenues • Permits up to 50% federal aid for new toll road construction • Permits loans and grants to public or private entities • Establishes congestion pricing pilot programme
NHS Designation Act (1995)	• Establishes state infrastructure bank pilot programme • Removes limits on advance construction and permitted flexible match • Makes interest and insurance eligible for federal reimbursement • Permits loans to non-tolled projects with dedicated revenues • Expands federal aid share of toll projects to 80%
Federal Acquisition Reform Act (1996)	• Allows accommodation of turnkey project delivery options
NEXTEA (**Administration Proposal 1997**)	• Proposes permission of toll interstates • Converts congestion pricing to value pricing programme and expands programme flexibility • Clarifies review of innovative finance in TIP development • Provides funds for federal credit enhancement for nationally significant toll projects • Establishes/funds SIB programme

The report sees PPP as a relatively new approach, mobilising combinations of different revenue sources and related financial methods with required supporting departures from the conventional road development process. Objectives vary from project to project and within programmes, but are defined as being:

- additional finance generation above and beyond conventional methods, in the face of general increase in capital needs;
- accommodating important but expensive improvement projects;
- controlling (eliminating) cost overruns, given limitations by tax revolts and politically constrained budgets;
- "fast tracking" project development to accommodate/match service needs and to respond to the pace of needed economic development and other land use programmes;
- avoiding extended procurement and disruptive phased build-out cycles;
- improving efficiency and performance in terms of integrating life-cycle economics and quality assurance;
- responding to customer markets for special services (such as hot lanes or inter-modal facilities);
- operating the systems in real time to minimise incident effects;
- accessing and deploying the latest technology for "intelligent systems" and longer life cycle facilities;
- obtaining a single point of responsibility for increased accountability;
- avoiding the necessity of adding staff in a downsizing environment.

The trend is to transfer risks to the party best able to control those risks, such as;

- having contractors bear the risk for project design and construction costs;
- completion schedule via turnkey contracts and incentives/disincentives;
- careful management of the project development process through private programme management;
- access to the latest financial technology expertise;
- outsourcing of road operations and maintenance.

All of the above involve changes in the roles of the public and private sectors, with the allocation of project risks and rewards in the most realistic and cost-effective manner while still protecting private and public partners; basic non-project objectives.

According to the article, PPP approaches range from conventional finance and delivery (but using the full financial and project delivery flexibility now within the federal aid programme) to fully privatise toll roads at the other extreme. They also include such hybrids as ISTEA-based developer-sponsored PPP's with public-resource sharing, the non-profit variant, and innovative public authority toll roads. The principle features of these models are compared as follows:

- Traditional free road with conventional funding/development (encompassing traditional major road development)
  -state agency owner and developer
  -private firm provides limited services for fees
  -tax funds (capitalising on new federal flexibility)
  -pay-as-you-go project segments
  -sequential design/bid/construct on a lowest cost bid basis
  -project permitting public
  -all risks public

- Advanced "free" road using innovative finance/turnkey project delivery (focused on large road reconstruction projects such as I-15 Salt Lake)
  -state agency owner and developer
  -turnkey fixed-price design/construct and maintenance with incentives or disincentives
  -innovative finance possibly including debt finance against public tax fund guarantees
  -project permitting public
  -all risks public

- Innovative public toll road (focused on large new road projects such as the TCA toll roads in Orange County, California)
  -state/local agency as owner developer
  -revenues from users/beneficiaries (tax-exempt debt)
  -mix of toll revenues, assessments, state/local funds as loans/grants/credit
  -private firms provide some (turnkey to full finance/DBOM) services for a fee
  -private entities may defer payment or take equity as part of fee
  -project permitting public
  -most risks public; private contractors may risk fees, some equity

- Non-profit community association developer toll road (increasingly used in several PPP projects in Washington, Arizona, Minnesota, South Carolina, and Virginia)
  -community non-profit corporation as owner developer
  -revenues from users (tax-exempt, toll-backed debt)
  -mix of toll revenues and state/federal/local funds as loans/grants/credit
  -private firm provides multiple services (finance/DBOM) for a fee
  -private firm may also take deferred compensation
  -local government role as sponsor
  -financial advantage of tax-exempt debt
  -project permitting public
  -most risks public; private sector may risk fees

- Private/developer sponsored toll road (used in Dulles Greenway and SR-91 Expressways in Orange County, California, and is under negotiation for several larger projects)
  -private firm as owner (finance/develop/operate/maintain on a BOT or BTO basis) participating in project revenues (or losses)
  -revenues from users/beneficiaries (toll-backed, taxable debt)
  -mix of toll revenues, assessments/contributions, and state/federal/local funds as loans, grants or credit
  -finance with developer equity, venture capital, taxable debt
  -public sharing of total project cost or some component such as permitting
  -turnkey design/build contract
  -all or most risks private

The author acknowledges that there has been slow progress in moving PPP projects to implementation, in part relating to the limited candidate projects. Whereas early PPP's were "Greenfield" projects where resistance to tolling was not encountered, more recent candidates have begun to focus on logical targets for new forms of finance and partnership.

<u>There has been enough experience to identify some of the key issues suggesting that serious, robust, long-term programmes will involve continuing institutional evolution to prepare for change in functions, roles, relationships, risks, and rewards at all levels. Policy and legislation is again seen as crucial, and has aimed to:</u>

- Seek and develop new forms of agreements with public and private entities (including outsourcing, franchises, etc.);
- Use partnerships for a wide range of transportation improvements (including roads, improvement, new technology);
- Use private and public entities to conduct the complete range of necessary activities and new roles;
- Use new forms of finance (including tolls and private equity commingled with state and federal funds, pricing);
- Execute new forms of contractual arrangements such as outsourcing, turnkey, franchising and product selection, and procurement processes (RFPP, negotiation, and competition).

There has been an iterative relationship between project agreements and improved legislation that indicates that many of the issues later encountered at the project level are better handled in enabling legislation. Key issues that project experience suggests need to be covered in enabling legislation include the following:

- ability to impose tolls;
- pilot programme versus programme integration authorisation;
- ability to commingle federal, state, and private funds;
- exception from conventional procurement;
- ability to award exclusive franchises;
- exercise of eminent domain and granting of other property rights;
- state versus local project review authority and related opportunities for community involvement;
- private use of public right of way;
- ability of sponsor to impose fees and tolls;
- exclusive rights to provide a public service for profit;
- protection of private-sector project concepts (intellectual property);
- conformance with applicable state standards and criteria;
- rights in ownership and spatial and temporal extent;
- non-compete clauses.

According to the text, budget and programme are interrelated with programming, reflecting the availability of resources and public and political support. New resources and project delivery methods can, in some cases, support such otherwise unfeasible projects.

A1.12 Malmberg-Calvo, C (1998), *"Options for Managing and Financing Rural Transport Infrastructure".* World Bank Technical Paper No. 411, Washington DC

This report examines the transport issues of rural villages in Sub-Saharan Africa. Most trips made in rural Africa (87%) are on foot, with 65% of household time and effort being spent on transport. Issues relating to women are also examined in some detail. These statistics and those relating to the state of most of the road system lead the author to conclude that there is huge scope for investment and improving transport services, with emphasis on intermediate transport.

The author has no doubt of the close link between isolation and poverty, especially in view of the fact that 70% of the regions people live in villages that are dependent on rugged roads, track, and paths in order to perform their daily tasks. This local transport network carries a third of the regions GDP. Lack of consideration given to the condition of access has meant that government rural roads in the region that need to be rehabilitated or replaced will cost US$ 48 billion.

Calvo believes that the strengthening of local institutions is they key remedy, with the management of rural transport being locally specific.

The paper proposes a framework for improving the managing and financing of local government roads and community roads and paths, based on a public-private partnership of cost-sharing between all vested parties. The author also feels that devolving ownership to small-scale farmers, the largest private sector group in most of the region will increase efficiency and bring more roads under regular maintenance.

A1.13 National Research Council – Transportation Research Record 1107
Private Sector Involvement and Toll Road Financing in the Provision of Highways

A1.13.1 *Goldstein, A,* "Private Enterprise and Highways"

Based on circumstances in the UK, the author believes that there seems to be no compelling case for the use of anything other than private enterprise on the main highway network. For design and construction, the report implies that where private enterprise is already extensively developed there appears to be further scope for trials of funding by the private sector with revenues from government based on the usage of the highway.

For highways generally, if government can underwrite the statutory requirements, there may be scope (but if so it would be modest) for increasing the contribution of the private sector to the pre-construction stage activities. The market alone cannot supply highways in the UK.

The report notes that government could limit itself to the provision of statutory powers for the selected enterprise and the enactment of regulations – including if thought necessary the setting of operational limits, such as maximum unit tolls. The second kind of government involvement is the provision of statutory powers and entry into the public-private mix of activities. The report then indicates what the author believes to be the advanced main advantages of greater privatisation, namely:

- The same outputs would be achieved with less input as measured by money, time, or physical units (productive efficiency).
- There would be less misallocation of resources, hence less economic distortion through greater use of the market mechanism (allocative efficiency).
- Funding would be external to the Treasury exchequer (i.e. not included in the PSBR) and therefore more roads would be built, or roads would be built earlier than would otherwise be the case, to the benefit of the community.

A1.13.2 *Mitchell & Botha,* "Financing, Private Sector Involvement, and Market Processes in the Provision of National Roads in South Africa"

There is general concern expressed over the gradual decline in revenue for road financing, as well as severe inflation in road construction costs resulting in an overall cost-revenue squeeze. Additional problems are identified, such as the siphoning-off of road building funds to uneconomic multi-modal transportation schemes, and the rising maintenance and operating costs on the more highly trafficked facilities.

In order to identify appropriate levels of road expenditure, as well as an aid to the rational allocation of funds to various projects, the DOT (1980) initiated a countrywide road needs study, confirming the inadequacy of funds for road construction to meet the country's road traffic demands.

Thus in 1986 a Toll Road Scheme was introduced and tenders were put out and received for complete financing, construction and operation of certain toll road projects over a period of 25-30 years, with the facility to revert to government control after expiration of the particular project or franchise. The two chosen consortia controlled around 80% of total private road building strength, raising fears of monopolistic behaviour. Financial guarantees were required, and at the time some form of statutory body was identified as a need for control of toll roads and that until all aspects had been fully considered, government control would remain significant.

Disadvantages and/or difficulties were identified: mainly that private enterprise is essentially based on self-interest and that development is run by profit. The role of government is seen to change to that of arbitrator between private and public interests – although its information will be coming from the well-informed parties, all of who will have vested interests.

It is recommended that governmental approach should be one of caution as constraints can always be lifted or relaxed but not easily imposed later. The basic aim in this case, says the author, is to obtain funds from the private sector at a reasonable cost and on a regular long-term basis. The entrepreneurial aim appears to be to limit equity during the earlier stages of a project and then, as returns improve, to expand the loans. But these loans are often large and have high degrees of risk, especially when high interest rates prevail. There are also elements of unavoidably long pay back periods, and that facilities revert back to governmental control at the end of the concession period.

The report then sets out what it believes is required to enable any proposed enterprise to be successful:

- Government must be in a position to ensure and to demonstrate that adequate facilities for the development of the country are provided in an accountable manner, and;
- Private sector institutions undertaking the provision of certain public facilities through privatisation must be able to access sufficient funds at a cost that will ensure that in the long-term, enterprise will yield adequate profits.

The author states that unless these conditions are met, any attempt to privatise roads will fail.

A1.14 *Private Finance Panel (1996),* "Practical Guidance on the Sharing of Risk and Structuring of PFI Contracts".

This report compares and contrasts PFI against public sector 'Capital Asset Procurement' (CAP) procedures. It examines many issues surrounding this including risk sharing in PFI contracts, the risk retained by the public sector, and the typical characteristics of a PFI contract. Under PFI responsibility for designing, building, finance and operations are transferred to the private sector.

Although private sector involvement through PFI is not universally applicable it can have a wide range of applications. A fundamental difference between PFI over CAP is the timing of responsibility and payment. For example under CAP:

- The public sector will employ consultants to prepare a detailed design or specification.
- The specification will then be put to tender for quotes, particularly on cost.
- The winning contractor or supplier will build the asset under public sector management (through a construction or supply contract) and be paid out over, say, 3 years.
- The asset will then be operated by the public sector.

In PFI contracts however:

- No longer does the public sector take responsibility for the design of a specification through consultants. It specifies (with consultants to advisers) its service requirements.
- No longer does the public sector manage a construction contract, it waits for its prescribed service through the PFI services contract. The private sector manages the contract.
- No longer does the public sector pay capital over the construction period, it pays for the service on receipt and only on receipt. The private sector pays the capital costs that it recoups through service payments.
- No longer does the public sector operate the asset; it monitors service delivery and performance.

A1.15 "Privatisation and the Emerging Private Sector in Russia", JUNE 20-21, 1994. Synopsis of Conference Proceedings, World Bank Studies of Economies in Transformation

A1.15.1 An Overview of Russian Mass Privatisation
Boycko, M. Russian Privatisation Centre

The main goals of the Russian Mass Privatisation Programme (MPP) – which began in December 1992 – were to transfer of State-Owned Enterprises (SOE's) to the private sector, to remove the political control of firms, and to create a constituency for a market economy. To some extent this has been successful.

It is noted that insiders dominate the ownership structure and as a result secondary trades have begun to take place. The main goal identified, now that so much reform has been undertaken, is to focus on attracting foreign investment.

A1.15.2 View of the Private Sector and Entrepreneurship in Russia Today
Filippov, P. Administration of the Presidents Office, Moscow

Misleading information and fraud are a major problem in the private sector. Often firms show signs of reform on the surface, but in reality have little commitment to the new system.

One of the main obstacles to reform is people's mentality, which can only be changed by effective advertising and education programmes. The author feels that ultimately the future of reform may well collide with traditional Russian psychology, and that it is up to international parties to ensure that a fatal collision does not occur.

A1.15.3 The Next Sages of Reform in Russia
Schleifer, A. Harvard University

The development of more comprehensive property rights laws and curtailing the power of organised crime are identified as being key considerations. The author also identifies other points deemed important, and they include:

- Move to cash privatisation to attract capital and create more core investors.
- Implement legal reforms, particularly in commercial law, to allow law and government to replace the Mafia.
- Privatise and register land and urban real estate.
- Further development of corporate governance functions.
- The development of securities markets, so shareholders can exercise their most basic governance power, such as exit rights.
- Development of a social safety net to prevent enterprises from using social assets as an excuse to extract government subsidies.

A1.15.4 Regional View of Privatisation – Primorsky Krai Region
Vacroux, A. GKI

Most privatisation in this region, which is rich in economic variables, occurred through competitive tender with restrictions forbidding the new owner to change the line of business for a period of five years – a major problem in other regions.

Problems did occur however. There were disputes between regional and municipal governments regarding ownership, and 're-profiling' had occurred despite every effort to prevent it. The firms that re-profiled drove up prices, even sometimes closing temporarily to enable labour collectives to develop business strategies. The struggle between many of the vested parties resulted in many enterprises forming defensive structures to protect themselves from outside investors, seeking to transform the economic power of industrial enterprises into political power.

A1.15.5 Private Sector Development in Russia
Webster, L & Sheppard, M

The sector is described as being heterogeneous, composed of new firms, newly privatised SOE's, and firms which have been operating in a quasi-private mode. In the survey, undertaken in November 1993, it was shown that managers tended to be male, well-educated, skilled people who have gaps of knowledge in a number of specific areas relating to operating a private business.

New firms tend to have a 'quick-buck', very short-termism outlook, with newly privatised firms looking to the longer-term. New firms tend to be flexible and adaptable, and able to take advantage of the inefficiencies commonly associated with SOE's, although an SOE tends to be a better guarantee of delivery. On the whole, private firms tend to avoid large investments and most is equipment leased. Avoidance of full-time employment and long-term finance is another feature, instead relying on short-term loans and customer advances for working capital.

To improve the situation, the author recommends more trade liberalisation to encourage more competition, with practical training (not just theories) proving very desirable. Constraints to business development need to be identified and ranked, addressing first those with the greatest commonality.

A1.16 Riverson, Gaviria & Thriscutt (1991), "Rural Roads in Sub-Saharan Africa". World Bank Technical Paper 141, Washington DC

This report looks at the following issues: review of Bank experience, planning, design and technology, resource mobilisation, sectoral organisation and institutional performance, bank project management, and policy recommendations.

With regard to rural transport services, it is recognised that improvements to transport infrastructure serving rural areas have not necessarily been followed by increased availability and efficiency of transport services for goods, as well as for people. Chronic shortages of fuel resulting from inadequate pricing and marketing policies have affected rural areas most severely, as well as deficiencies in tariff regulation and parastatal control. The report recommends more attention should be given to policies affecting the availability and cost of transport services at the local level, and also considers intermediate modes of transport, which are generally underdeveloped.

Improvements would have to be sought through changes in transport technology, especially alternatives to head loading (wheelbarrow, bicycle, animal draft, power tillers, etc), improvement in off-road structure and changes in post-harvest practices (processing and storage).

A1.17 World Development Report (1994), *"Infrastructure for Development"*. The World Bank, Washington DC

The main elements of the report are as follows, where sections 2,3 and 4 are of particular interest:

1. Infrastructure: Infrastructure: achievements, challenges, and opportunities;
2. Running public entities on commercial principles;
3. Using markets in infrastructure provision;
4. Beyond markets in infrastructure;
5. Financing needed investments;
6. Priorities and implementing reform.

Section two looks at the practicalities of running public entities on commercial principles. It indicates that much change is needed before methods put into place can work; i.e. the need for a 'pro-development' environment. Other key considerations identified include coherent goals focused on delivery of service, management autonomy with both managers and employees being accountable for results, and that successful providers of infrastructure (private or public) are usually run on business-like principles.

Importance is also attached to financial strength, where tariffs cover (minimum) operation and maintenance requirements, while effective cost-accounting will control expenses. In addition the author believes that the close examination of failure is essential so that mistakes can be learned from. A survey of forty-four countries with

World Bank-financed projects designed to improve infrastructure performance revealed the most common problems in six infrastructure sectors.

Common management problems in public sector infrastructure entities, 1980-92
(Percentage of World Bank loans in which conditions were imposed to address the problem area)

Sector	*Number of Loans*	1.17.1.1.1Unclear goals	*Lack of autonomy and accountability*	*Financial problems*	*Wages and labour problems*
Electricity	48	27.1	33.3	72.9	31.3
Water	40	25.0	40.0	70.0	35.0
Telecom	34	14.7	35.3	52.9	32.4
Rail	39	15.4	20.5	53.8	33.3
Road	35	8.6	22.9	40.0	40.0
Ports	28	21.4	35.7	32.1	42.9

Source: World Bank database (ALCID).

By creating organisations driven by commercial principles, says the report, governments can avoid the four common problems and increase chances of success. It is noted that although corporatisation insulates organisations from many government constraints and pressures, it does not mean that infrastructure providers are able to set their own agendas and goals.

This is the responsibility of government, as is the regulation of behaviour, so as to ensure an adequate return on society's investments. The introduction of competition with appropriate regulation is the missing element for success, as simply establishing commercial principles and maintaining them through political commitment are not sufficient for the success of commercial enterprises.

Chapter three notes that the weight of evidence shows competition in or for a market for services is generally more effective in responding to consumer demands than are mechanisms for making public enterprises more accountable. Tailored contracts and sensible risk sharing arrangements are also required. In addition the report points to the use of consumer feedback in 'innovative' ways in the regulatory process as an important priority for regulators.

In Chapter four the report looks at decentralisation and participation issues, improving budgetary allocations, subsidies and transfers to the poor, and addressing externalities.

The conclusion states that improving infrastructure performance is often difficult – politically, technically, organisationally, and administratively – and that without the fundamentals of governance – accountability, a predictable and stable legal framework, openness, and transparency – even the best efforts can go astray. There is also a need to achieve a balance between expert and user, and between direct and indirect goals. In addition the choice of instruments and approaches must reflect sectoral needs and the capacities of implementing agencies.

A1.18 UNDP Website (1998), "Urban Public Private Partnerships". UNDP

The purpose of the programme is to promote collaboration between the private and public sectors in order to address some of the most urgent developing country problems. Project experiences are carefully monitored so as knowledge can be shared, as are elements of success so that they may be replicated and obstacles be avoided.

The UNDP believe that the central process is that projects should address local priorities and common concerns. By bringing together the collaboration in sustainable joint ventures, the result should be that all parties meet their objectives, and the local dwellers enjoy a higher quality of life.

Participants tend to be wide-ranging, each depending on the nature of the individual project in which they are collaborating. They believe that it also helps turn problems into a viable business opportunity, and whereby relatively small initial financial inputs can dramatically increase impact. Innovations of the programme are listed as:

- Using ODA to leverage private sector investments.
- A new type of project management - emphasising resource efficiency, stakeholder participation, replicability and, in general, a more comprehensive and sustaining approach to development.
- Establishing linkages between investment and capacity building – the lack of an enabling environment has often led to the failure of private sector investments. Insufficient revenue generation is also a problem, but if the environment becomes enabling, it is hoped that failure will be lessened.

The site also lists the project selection criteria for UNDP. In order to be eligible for selection, a project must:

- Focus on at least one of the following city services: water, sanitation, waste management or energy services.
- Address a problem that is a priority for local authorities and the central government, and also a common concern shared by other cities in the region.
- Establish a functioning public-private partnership, not simply the privatisation of city services. Public administration must have an active interest and participation in the project.
- Demonstrate a strong potential - including the possibility of reasonable profitability - for attracting the private sector.
- Provide an opportunity for improving local social conditions through job generation, improvement of city services and enhanced urban living conditions.
- Respect local cultural values and established labour traditions.
- Embody opportunities for technology transfer and capacity building.
- Involve local stakeholders, non-governmental organisations and community based organisations in project development.

In identifying private sector partners to participate with municipalities in mixed capital companies, the programme uses a transparent process based on clearly defined criteria. In order to be eligible for selection, the private partner must:

- Be willing to contribute to the cost of the projects pre-feasibility and feasibility studies.
- Be prepared to invest in the new company when it is formed.
- Have experience operating the eco-efficient technologies to be used by the new company.
- Have experience operating in the country where the new company will be established.
- Have the support of its own government's development agency.
- Strongly support and advocate eco-efficiency and local participation.

A main theme running through is **Participation and Shared Responsibility**, that is a unique international network - not a new institutional bureaucracy.

Benefits of Involving Private Sector Partners to Deliver Urban Services

"The experience of privatisation in developing countries to date indicates that private corporations, NGO's and informal sector enterprises have potential advantages over government agencies in providing some type of services. The private sector can provide lower production costs, more efficiency in service delivery and has greater capacity to maintain capital equipment. Private companies can often offer consumers greater choice - and make decisions faster and more efficiently- than public bureaucracies.

They have access to the latest technological advancements and can undertake their own research, allowing for more flexibility in adjusting the types and levels of services to changing needs. They can also reduce financial burdens on governments for wages, operating costs, debt servicing and investment. Today, more than $120 billion of private international capital flows into developing countries. Yet little of this is specifically directed at meeting social needs through environmentally sound approaches. One of the main objectives of this programme is to re-direct a percentage of these investments in this direction."

A1.19 United Nations Industrial Development Organisation (1996), "Guidelines for Infrastructure Development Through Build-Operate-Transfer (BOT) Projects".

The book states that in such projects, lenders look to the profitability of the scheme in terms of the projects assets and revenue stream for repayment, rather than the traditional governmental guarantees or the assets of the project sponsors.

Potential advantages to the host government of using the BOT approach for infrastructure development

- Use of private sector financing to provide new sources of capital, which reduces public borrowing and direct spending and which may improve the host government's credit rating.
- Ability to accelerate the development of projects that would otherwise have to wait for, and compete for, scarce sovereign resources.
- Use of private sector capital, initiative and know-how to reduce project construction costs, shorten schedules and improve operating efficiency.
- Allocation to the private sector of project risk and burden. The private sector is responsible for the operation, maintenance and output of the project for an extended period (normally the government would receive protection only for the normal construction and equipment warranty period).
- The involvement of private sponsors and experienced commercial lenders, which ensures and in-depth review and is an additional sign of project feasibility.
- Technology transfer, the training of local personnel and the development of national capital markets.
- In contrast to full privatisation, government retention of strategic control over the project, which is transferred to the public at the end of the contract period.
- The opportunity to establish a private benchmark against which the efficiency of similar public sector projects can be measured, and the associated opportunity to enhance public management of infrastructure facilities

It is emphasised that each project is different and will require differing degrees of government support depending on the type, size and complexity of the project and the host country's economic and regulatory conditions. It was noted that political and economic uncertainties pose additional obstacles to the BOT approach.

Host government direction and support (legislative, regulatory, administrative and sometimes even financial) are essential in most developing countries.

Formula for success (as identified by UNIDO):

- Feasibility study must conclusively indicate financial and economic viability over the project lifetime and under different scenarios.
- Country risks should be manageable, and there should be strong governmental support (i.e. project must rank highly on host governments list of infrastructure projects), as well as a stable legal framework.

- Bidding procedure must be fair and transparent - experience shows that this will normally result in terms and conditions more favourable to the national interest.
- BOT transactions should be structured so as to be concludable within a reasonable time and at a reasonable cost.
- Sponsors must be experienced, reliable and have sufficient financial strength, as should the construction contractor. Risk should be rationally allocated among all parties.
- Currency, foreign exchange and inflation issues must be solved.
- BOT contractual framework should reflect the above, and the public and private sectors need to co-operate on a win-win basis.

A1.20 The World Bank (1996), **"Development In Practice – Sustainable Transport: Priorities for Policy Reform".** *World Bank, Washington DC*

The publication states that there are a wide variety of considerations that are important to sustainable transport for development, including re-focusing transport sector policy, economic, financial, environmental and social sustainability, and re-defining the role of governments in the transport sector.

The section relating to Economic and Financial Sustainability is particularly relevant, with consideration given to private ownership and operation, private operation within a framework of public control, as well as making public sector management more market-sensitive.

The report details macroeconomic World Bank studies that show that investing in transport promotes growth by increasing the social return on private investment without crowding out other productive investment. Microeconomic analysis confirms a high social value of transport, with economic return being 22% (half as high again as the bank average). It was shown that improvements to rural transport lower agricultural costs both directly (through increasing access to markets and credit) and indirectly (through facilitating the development of the non-agricultural economy).

The report notes that improvements to inter-urban transport have facilitated domestic and international trade and sped the movement of freight, as well as of people. Again one notes the importance attached to learning from experience. For example, the physical completion of projects does not itself generate the expected benefits if institutions are weak and policy framework is inadequate.

Encouragingly from the point of view of PPP, the report shows that dominance of the public sector in transport services operations often results in costs being too high, tariffs too low, and thus higher public deficits.

It is emphasised that work is still needed in relation to extending basic infrastructure networks and providing for their adequate maintenance. Appropriate strategies and actions will be required both to improve provision and maintenance of transport *infrastructure* and to improve the provision of transport *services* using that infrastructure.

Overall, the author feels that the challenges highlight an overall need to reform transport policy in order to support a better quality of life on a sustained basis. The report then lists three types of Bank action that are most important in support of policy and institutional reform to enhance sustainability:

- Synergy among the different dimensions of sustainability.
- Urgent action on basic reforms.
- Employment of relatively novel actions, such as measures to assist NMT.

The objective is seen to be to increase the responsiveness of transport supply to user needs by creating competition and by enhancing user participation. The Bank believes transport is central to development, and that it is essential to confront the crisis of inadequate asset maintenance. Without physical access to jobs, health, education, and other amenities, quality of life suffers; without physical access to resources and markets, growth stagnates and poverty reduction cannot be sustained.

The report points out that poorly designed policies and strategies often merely serve to aggravate the problems of the poor, harm the environment, ignore the changing needs of users, and exceed the capacity of public finances.

It also notes that involving the private sector to alleviate problems is easier in some sectors, such as telecommunications, than others, such as transport. The specific characteristics of the different transport sub-sectors affect the potential for expanding the role of competitive markets.

ANNEX 2 PPP CASE STUDIES

The following are examples of attempts at PPP approaches from different sector.

A2.1 UNDP WASTE MANAGEMENT PROJECTS

A2.1.1 Urban Waste Management Project: Ahua Pura, S.A. Manizales, Colombia

Addressing water supply and quality and problems caused by coffee producers (by use of a traditional, highly polluting coffee washing process), as new company comprised of several government agencies and private sector companies was formed in an attempt to create an economically viable solution to the pressing environmental problems. The company has developed a complete business plan for domestic solid waste collection, disposal and recycling that will extend out to encompass several municipalities and thousands of households and businesses.

A2.1.2 Textile Industry Relocation/Park Pollution and Waste Management Bandung, Indonesia

In an attempt to create a sustainable waste management system that incorporated the use of zero emissions technologies, a partnership between two private sector companies and three public agencies was established. Part of the project includes the introduction and promotion of "cleaner" technologies to control pollution in industrial parks.

A2.1.3 Greater Tunis Packaging Waste Disposal and Recycling Project - Tunis, Tunisia

This project is concerned with finding an economically viable solution for waste disposal and recycling in the greater Tunis area. A partnership between a few local government agencies along with firms in the packaging industry was created to provide infrastructure services that include the collection, sorting and recycling of packaging waste (paper/cardboard, glass, aluminium, etc.) to sell to re-users.

A2.1.4 Bursa Municipality Integrated Waste Management Project - Bursa, Turkey

The scope of this project is broad as it is an attempt to find economically viable options for a number of different waste management schemes including urban domestic waste, packaging recycling, industrial waste, toxic/hospital waste, materials recovery facility and waste energy biogas among others. The partners are made up of the municipality of Bursa and Cevko as principle partners, as well as other local and national governmental agencies and private companies.

A2.1.5 Energy and Environment Management Enterprise - Willowvale Industrial Park, Harare, Zimbabwe

The recent increase in the development of industrial parks in Zimbabwe was brought to the attention of SPM/UNDP to seek a solution to the growing environmental

A2.4.1 Portales, New Mexico

Many public and private agencies in New Mexico are co-operating with each other to promote the programme. Their initial investment includes educational materials tailored for specific local conditions, with five communities already involved in the process.

A group of eleven economic development partners from New Mexico constituted the largest team at the WRDC training. They represented some of the organisations that have formed the New Mexico Rural Economic Assistance Link (REAL). The resulting programme that was put in place in Portales helped double revenues and increase the employment base of a local peanut processor to the equivalent of approximately 50 full-time employees.

Many of those involved believe that the existence of the project has at least in part been responsible for the location of a milk processing plant in Portales (Mid-America Dairyman, Inc.) employing 15 people, a new trucking firm that transports the milk employing 126 people, and an additional 300 on-farm jobs on dairies producing milk to supply to the new plant.

Working from the WRDC documents, New Mexico produced a customised set of training manuals specifically adapted for the conditions in the state. Two videotapes have been produced that document the Portales programme for interested communities. Five New Mexico communities have received assistance from REAL in the past two years to conduct business retention and expansion programmes. The programme received the Arthur D. Little Award for best overall economic development programme in the US from the American Economic Development Council.

A2.4.2 Montana

One of the pilot states in operation for four years, it is funded almost exclusively through the Extension Service with primarily in-kind contributions from the eight participating communities. The success here has attracted recognition from state government.

During the past five years the Montana Extension Service has helped eight communities create or hold on to more than 1200 jobs through applications of the western business retention and expansion programme. During the lifetime of the project one counties licences rose from 379 to 518 between 1989 and 1994. The success of the project has resulted in the State Governor requesting that the programme be expanded to assess state wide potential. The Governors plan was to visit 100 of Montana's major employers during the 1994-95 winter.

A2.5 Transport in Rural Wales
Countryside Commission for Wales (CCW)

The publication is based on responses to consultation exercise, undertaken by CCW between November 1994 and February 1995, which created a wide debate on rural transport issues with a range of interested organisations and individuals. CCW aims to:

Continue to explore with partner organisations;
Encourage recreational cycling;
Encourage partners to ensure that buses and trains meet the needs of users;
Support well designed traffic calming measures in villages;
Give examples of good practice that may be followed elsewhere, such as;

- Snowdon Sherpa recreational transport scheme (oldest in UK)
- Cambrian coaster train service linking remote rural villages
- Detailed timetables of all services in the area (Gwynedd)
- Refurbishment of rail stations and provision of park and ride schemes

The Chief Executive of CCW feels that work implemented should be realistic and workable, and that policies should be built on a wide-ranging consultation exercise. If this is done effectively, he believes that the work will "...contribute towards the protection and enhancement of landscapes, wildlife, and people's quality of life".

A2.6 EXAMPLE STATE MODELS OF PUBLIC-PRIVATE PARTNERSHIPS – UNITED STATES

Reported in Lockwood, S (1997), *"Public Private Partnerships are the Answer: What is the Question?"* Transportation Finance for the 21st Century - Proceedings of a Conference - Dallas, Texas April 23-25 1997 Transportation Research Board, USA

INSITUTIONAL ISSUES	ARIZONA CH.25 Arizona Statutes (as amended in 1995)	CALIFORNIA Ab680	CALIFORNIA Orange Co. TCA	MINNESOTA CH. 160 Minnesota Statutes	VIRGINIA Public/Private Act of 1995	WASHINGTON Title 47
INSTITUTIONAL ROLES AND AUTHORITY	Arizona DOT administrators Unlimited (solicited or unsolicited)	CALTRANS administrators Up to 4 projects	Joint Powers Agreement of local agencies	State road authority and agreement with private operator. Final approval DOT Commissioner	Qualified local agencies can contract	Washington DOT administers
FACILITY OWNER/DEVELOPER/ OPERATOR	Public owner private developer/operator	Public owner, private developer/operator	Public owner, private developer/operator	Public owner, private developer/operator	Public owner, private developer/operator	Public owner, private developer/operator
ROLE OF PRIVATE SECTOR	BTO – lease term negotiable	Leasehold interest – 13 to 35 year lease term	Construction, management, operations	BOT or BTO or BOO	No predetermined model	BTO preferred BOT possible lease term up to 50 years
INNOVATIVE USE OF FEDERAL FUNDS	Yes	No	No	Yes	Yes	Yes
EMINENT DOMAIN	DOT can exercise on behalf of developer	CALTRANS can exercise on behalf of the developer	TCA has power	Available to "road authority"	Any public entity can exercise on behalf of the developer	DOT can exercise on behalf of the developer
TOLL RATE SETTING	By transportation board – if solicited May utilise HOV lanes	Negotiated in agreement "reasonable returns"	By TCA	In development agreement – may utilise time of day pricing	Negotiated with responsible public authority	Negotiated in agreement with DOT secretary
ALLOWABLE RETURNS	Reasonable	Reasonable Incentives available	Only to pay for construction and tax collection	"Reasonable rate of return"	Reasonable, costs subject to review for reasonableness	Reasonable rate of return – maximum established. Incentive with sharing possible
DEBT INSURANCE	Taxable	Taxable	Tax exempt	Either	Taxable	Taxable or tax-exempt
COMMINGLING OF FUNDS	No	No	Yes (through special legislation)	Yes	Yes – established toll revolving loan fund	Yes – revolving loan fund possible grants & other innovative financing agreements
ROAD ALIGNMENT	Reasonable – "at least direct as alternative route"	"Offer alternative route selection"	Parallel to other public thoroughfares and highways	Can be vetoed by local jurisdiction	Can be rejected by any local jurisdiction	Affected jurisdiction involved and consulted
ORIGINATION	Solicit proposals	Solicit proposals to "take advantage of private efficiencies"	Local agency	Local road authority solicits proposals	Application to State commission – no limit on number of projects – unsolicited proposals accepted	Solicitation
PROCUREMENT PROCESS	Negotiated	Negotiated	Does not apply	Negotiated	Public procurement act shall not apply	Negotiation

ANNEX 3 BUS DEREGULATION IN THE UK

In order to examine the case for PPP in rural transport provision in developing countries, it would be useful to examine the issues arising from other attempts to modify bus service provision. In this annex UK bus deregulation is considered in detail together with experiences from other countries.

Information on the UK experience was principally drawn from a series of reports from the Transport and Road Research Laboratory/Transport Research Laboratory. Key authors referred to are Balcome (1987) and Astrop (1993). Much of the international material is drawn from Cox, Love and Newton (1997).

A3.1 Background

Bus deregulation in the UK was initiated through the Transport Act 1985. It abolished the quantity control of bus services in the UK (outside London), services not registered commercially could then be put out to tender and subsidised by a Local Authority (LA) where it was considered necessary. Prior to the implementation of the 1985 Act there was very little competition in rural bus services.

Following deregulation freedom was given to operators to register and run on the routes they chose, (provided they fulfilled certified criteria) and set their own fare levels. Prior to deregulation cross subsidisation of routes had occurred however under deregulation it was no longer allowed. In general, if an LA wished to subsidise a service then it had to let out the route to competitive tender and it was able to specify the service frequency and the fares. As temporary incentive (from 1986 to 1990) a rural bus grant was provided to the operator direct from the Department of Transport. For very small contracts Section 5 of the Act did allow subsidies with out competitive tendering under the "de minimis" condition.

A3.2 The Overall results of Deregulation

Literature shows that important cost reductions have been achieved in many cases, where deregulation has been introduced (Heseltine and Silcock, 1990; White, 1990). Table 1 shows that since deregulation service provision has increased, and costs have declined. Comparative results are shown for London which in the last few years has been moving towards competitive tendering.

Table 1. London & Outside London Results (1986-1995)
(London: competitive tendering. Outside London: deregulation)

Indicator	London	Outside	Combined
Total Costs	-23.5	-28.9	-27.1
Service Kilometres	30.4	28.6	28.8
Unit Cost (per KM)	-41.4	-44.7	-43.4
Passengers	1.3	-27.5	-21.6

Source: Cox, W, Love, J & Newton, N (1997), Outside London overall operating costs per vehicle km have declined by 45 per cent (inflation adjusted) and a major increase in efficiency in the use of manpower has occurred.

In a study of four representative Shire counties Astrop (1993) found that although the number of passenger journeys fell by 11% (1987-1991), level of service (measured in bus hours) increased in all counties bar Cambridgeshire, where there was a slight reduction in rural transport service levels. The changes were not uniformly distributed with increases and decreases from place to place *within* counties - and complete withdrawal of services occurred in some cases. Improvements tended to be associated with locations in or on routes to more major rural settlements. As far as it was possible to calculate, the cost of subsidising the network since deregulation was reduced by 26.7% in real terms, with little effect on the overall provision of service.

Since only a small proportion (less than 25 per cent) of bus operating costs were financed by subsidy, quite small overall cost reductions could produce relatively large subsidy reductions on the scale of those recorded. It is therefore possible that many operators will be able to run viable services without subsidy, or at the prices they have tendered. On the other hand, this 'gearing effect' could work the other way: small underestimates of costs, or small overestimates of revenue, could produce proportionally much larger deficits and eventual cancellation of commercial registrations and subsidy contracts, creating and increasing subsidy requirement.

Table 2 The level of Subsidies

COUNTY	Cost of Subsidies (£) 1986/87	Cost of Subsidies (£) 1991/92	Out-turn (£) 1991/92	Saving* in real-terms (%) 1991/92
Northumberland	528 000	598 000	555 000	11.8
Shropshire	746 000	828 000	905 000	25
Hampshire	3 968 000	4 270 000	3 970	24.7
Cambridgeshire	950 000	1 586 000	1313	26.7

Source: Astrop, (1993)

Competition for contracts for the subsidised routes seems to have had the effect of producing tender prices which compare very favourably with previous subsidy levels, so that most LA's found costs of subsidising all of the services for which they invited tenders were comfortably within their budgets, and there was no necessity to abandon low priority services. So although details of service may have changed, success has been achieved by and large in preserving service - even though the popular thinking was that this would be impossible.[1]

[1] The most significant changes occurred in the metropolitan areas, where attempts were made to reduce expenditure.

Subsidy requirements varied enormously between authorities, with some reducing revenue support by up to 70 percent, and others spending roughly the same, and very few with slight expenditure increases. It appears that these reductions in total revenue support requirements stem from operators' reactions to competition, or the threat of it.

A marked trend towards high-frequency minibus services was observed with improved access to residential areas. More frequent conventional bus services also occurred but mainly in urban areas and on inter-urban routes. Improvements in service levels and fares were often the result of competition between two or more operators.

Key negative results found included reductions in frequency, especially at times when demand was low and costs were high (early mornings, evenings, Sundays), and substantially reduced coverage of rural and suburban areas.

A3.3 Subsidy Policy

A great variety in subsidy policy was found between the different local authorities, with most change occurring in metropolitan areas. It is, however, possible to group types of adopted policy into several broad categories:

- to preserve the *status quo* - not possible to achieve in detail, so 'equivalent level' to pre-deregulation was sought;
- to provide 'adequate service' - apart from cases of over-provision, previous levels determined this anyway so there was thus a tendency to restore the status quo;
- the 'good housekeeping' approach - to cease subsidising services which provided poor value for money, often determined in advance of tendering advertisement.

In very few cases were authorities forced to make such cuts for budgetary reasons (LA were constrained by Central Government limits on their total expenditure) as most of the affected services could be accommodated within available resources. Block subsidy arrangements appear to have made identification of poorly performing services more difficult: it is easier to identify using individual service subsidy. Subsidy criteria are provided in Table 3.

Table 3. Subsidy Criteria

COUNTY	Service Subsidy Criteria
Northumberland	• Statutory – such as school; no minimum cost expected to be met from revenue. • High Priority - work, shops, health; 40-60% to be met. • Secondary Priority – evening, hospital visit, Sunday; 60-90% to be met. • Low Priority – general social, leisure and recreational; 80-100% to be met.
Shropshire	Considering school services and services for the elderly and disabled to be of high priority: • Service must carry at least 5 passengers. • Subsidy per passenger should not exceed double the maximum fare.
Hampshire	To qualify for subsidy, a service must show: • Sufficient demand: minimum of 3 passengers per journey in rural areas, 5 in urban. • Cost of subsidy should be no more than £2.50 per passenger.
Cambridgeshire	Where existing network could not be maintained, subsidy was given to: • Essential links to main centres and market towns. • Routes from residential areas to workplaces. • Links to educational establishments, shopping, recreation and health centres. • Services that have a proven need.

Source: Astrop, A (1993).

The process of 'gap identification' in services, although easier with the more simple pattern of the rural service, has presented significant problems to authorities. One method of 'gap identification' was to attempt to 'persuade' operators to amend their commercial services that were registered. - This is easy if the alternative is as commercially attractive as the original. Several LA's employed the use of 'de minimis' provision which allows them to pay a limited amount of subsidy to each operator without inviting competitive tenders. In certain cases this enabled authorities to negotiate small route or timetable changes with operators, thus either filling gaps or altering them so that they can be filled effectively by new services.

The alternative for the authorities was to invite tenders for new services essentially incorporating and extending commercial ones. Complications have arisen though, such as when an authority regarded the frequency of a registered service as inadequate, but could not sensibly enhance it without modifying the original. Often, subsidised services share parts of their routes with commercial ones.

Nevertheless, there is some residual competition between subsidised and commercial services, which may lead to adjustments in due course. In some cases the modified services are still operated commercially; in others, subsidies are paid to cover the net costs of changes.

A3.4 International Experience:

North America: approximately 10% of fixed route and more than 70% of door-to-door service is competitively tendered. In addition, 30% of US school bus service and more than 50% of Canadian bus services are tendered. All suburban bus service is competitively tendered in Montreal, while smaller public transport systems are competitively tendered in British Colombia, Alberta, Saskatchewan, and Ontario. More than 1,000 buses operate commercially into New York city from New Jersey.

Europe: the EU is encouraging conversion of public transport systems to competitive tendering: "*...the concession system (competitive tendering) - where services are subject to open tender but within a defined operational framework - is well suited to providing an environment which gives incentives to operators to raise standards whilst safeguarding system integration which is particularly important to urban and regional transport. The Commission...will look at ways of promoting the concession (competitive tendering) system.*"

Australia: conversions are underway or completed in Melbourne, Adelaide and Perth. Under a federal-state agreement, virtually all public transport services could be converted to competitive tendering by early in the next decade under a federal-state agreement intended to improve public resource allocation and international competitiveness by subjecting public services to competition.

New Zealand: New Zealand public transport systems have been converted to a regulatory system similar to that of the UK outside of London, most services being competitively tendered.

South Africa: more than 40% of work trips are carried by private operators using unsubsidised "kombi-taxis"; ownership of which has been one of the most important sources of capital formation for blacks. In the Johannesburg area, a bus-taxi lane has been built from Soweto to the downtown area.

Chile (Caracas, Santiago), and **Mali** (Bamako) - publicly operated bus systems have been closed and converted to commercial operation. **Sao Paulo** has similar plans. Santiago uses competitive tendering to award central city bus routes. **Seoul** has closed its public bus system, with all services now provided by private companies.

Istanbul and **Calcutta** are increasing the percentage of services provided by private operators. In many urban areas, private operators, especially mini-bus operators, carry the overwhelming percentage of passengers.

Table 4. Summary of Competitive Tendering Results (%) - all costs inflation adjusted

System	3.4.1.1.1	% Converted	Total Costs	Service Level	Unit Costs	Annual Unit Cost Change
Auckland	1990-96	100	-21.2	16.5	-33.5	-7.6
Denver	1988-95	25	3.0	25.6	-18.0	-2.8
Indianapolis	1994-96	70	8.5	38.4	25.9	-13.9
Copenhagen	1989-96	56	-18.5	5.0	-22.3	-3.5
Las Vegas	1993-94	100	135.0	243.0	-33.3	-33.3
London	1985-96	57	30.0	28.7	-45.7	-5.4
San Diego	1979-96	37	2.7	46.6	-30.0	-2.1
Stockholm	1992-95	59	-18.5	2.8	-20.3	-7.3

Source: Cox, W, Love, J & Newton, N (1997),

There are numerous examples of competitive tendering producing a quality transport service, which is imperative in assessing the success of the process. London transport found that competitively tendered service was generally of higher quality , and that when the public operator provided service in a competitive environment (faced with the threat of contract cancellation, like private carriers), service quality improved on the *same* services. Competitive tendering can also assist public agencies in fleet maintenance, by requiring contractors to provide vehicles of a specified standard.

Spain: In a comparison of private and public operators De Rus and Nombela (1996) found that public operators employed more labour and that wages were up to 18 per cent higher than private firms. The net result was that average costs were 42 per cent higher in public operators than private operators. It was predicted that very large benefits could accrue if public sector firms were privatised and if competitive tendering for route concession were allowed.

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ANNEX 4 MONOPOLY & CARTELS

A4.1 Introduction

Cartels can be see as any collusion between groups of companies to fix prices or control production to the detriment of the consumer and the wider market. Collusion can be either explicit or tacit, which in itself presents the problem of identification for the authorities. The law punishes the former, but from the economist's point of view (in Game Theory models of collusion), all that is needed is for the cartel members to have an "understanding" of how others will react to their behaviour. Tacit agreements can be self-enforcing, with theory providing no clear reason for exempting such collusion from the concern of antitrust.

A considerable measure of cohesion will be needed within the group if the cartel is to survive over a long period. Whether or not such cohesion is likely will depend in part on the number of firms. The larger the membership, the greater the difficulty of keeping everyone in line. If the price charged by the cartel attracts new entry, this will tend to increase the danger of instability, not only because of the increase in numbers but also because of uncertainty about how the newcomers will behave.

Australian Trucking Cartels
The argument rages around modern economics over the 'defence' of the cartel – that not all cartels are a bad thing. The $4 million fine of Express Trucking Company in Australia has led to one such argument.

An article in New Australian questions both the motive and the economic justification of the action taken. The author feels that the charges laid by John Fels, chairman of the Australian Competition and Consumer Commission were on the premise that price-fixing by companies is anti-competitive and detrimental to consumers' economic welfare. The argument is that through the work of von Hayek and Coase Theorem, economic theory will serve to dispel this belief. It is not necessarily true that in the absence of competition firms will see prices and output diverge from the competitive state. As long as 'contestable' markets exist, there should be no problem – but how does one define or even recognise a truly 'contestable' market? It is true that a monopoly/oligopoly/cartel situation can exist without detriment to the consumer, but monitoring of behaviour and price is essential to ensure the dominant position is not abused. The article argues, quite fairly, that so long as force is not used by a combination that harms competition and thus consumers (exploitation), then there is no cause for alarm.

Australian trucking companies formed a cartel-like arrangement, but the author feels that there was no anti-competitive action in this as others were free to compete against them – as Coase postulated, the firm exists in order to internalise certain market transactions.

The cost differences of members of the cartel will also play an important role. The smaller these differences, the more likely it is that price and profit allocation can be arrived at that is acceptable to all. The bigger the cost differences, however, the greater the danger of instability.

It may be argued that to collude effectively, firms must be able to:

- Reach an agreement;
- Detect breaches of the agreement;
- Punish firms that breach.

The more successful the cartel in raising prices, the greater the incentive to cheat, with this incentive being particularly strong at times when the market is depressed. Whether the firm actually decides to cheat depends on balancing the gains on cheating, against the costs, which depend on how likely the firm is to be caught and on what sanctions the cartel would impose. Factors such as seller concentration, homogeneity of the product, stable demand or the announcement of the lowest sealed bid, can and often do affect the ability to detect price-cutting breaches.

A4.2 Enforcing Restrictive Practice Policy

The effectiveness of anti-cartel/trust legislation is a function of its monitoring, enforcement and the resources devoted its achievement. Mechanisms need to be put into place that will detect, examine, and most importantly, deal with any restrictive practices.

In most developing countries anti-monopoly and anti-cartel activity is very limited. In most instances price control is the only effective measure. In the three most developed anti-trust systems of the world – namely the USA, UK, and the EU – there is no shortage of agreements to be investigated, with anti-trust authorities being able to initiate investigations into any sector or market where they have received complaints from the public who have been adversely affected by restrictions.

Monopolies and Mergers Commission – Cross-Solent Ferries

Case was brought in connection with the supply of ferry services between the Isle of Wight and the mainland of England. In 1990, Wightlink Ltd, a subsidiary of Sea Containers Ltd, carried 71% of passengers, 85% of cars, 94% of coaches and 80% of freight vehicles on the cross-Solent ferry services. A monopoly situation therefore exists in favour of Wightlink and Sea Containers.

Cross-Solent ferry services provide almost the sole means of transport for passengers, cars, coaches, and commercial vehicles to or from the Isle of Wight, and are an essential part of the infrastructure of the Island.

600 letters of complaint, predominantly from locals, were received about the level of fares. As there were no subsidies, the Commission felt level of fares must be considered in relation to the costs and profits of those services. However, although profits are substantial (12% of the replacement costs of its assets), the Commission found that neither the profitability of Wightlink nor its level of fares were sufficient in the current circumstances to be regarded as against the public interest.

Indeed, many aspects of the service have been to the benefit of their users, in particular an increase in capacity and usage of the ferry services over time, and the availability of cheap promotional fares. Island residents also benefit from some modest fare concessions. The report feels that the operators will no doubt recognise it as in their own interests to continue to improve some aspects of their services to meet users needs and alleviate some of the criticisms expressed to the Commission. They find insufficient grounds at present to justify the complaint that the ownership by ferry operators of port facilities and the difficulty of developing new port facilities would prevent new entry.

No current aspect of Wightlink's performance was found to be against the public interest but the competition it faces cannot be regarded as strong. The company remains in a dominant position which could be open to abuse and there may be need for further monitoring of its profitability and fares in the future.

Agreements are permitted in the UK and the EU, but only if they are registered and upheld. The main players in enforcement and administration procedures relating to competition are:

- EU Commission, and its Directorate General for Competition
- UK Restrictive Practices Court and the Monopoly and Mergers Commission
- US Anti-Trust Division of the Department of Justice, Federal Trade Commission.

The advantage of a judicial system is that it is open, with complaints laid at the EU approach for being too bureaucratic and arbitrary as it is prosecutor, judge and jury. Where the law against restrictive practices is less clear-cut the argument for economic rather than legal expertise in the judicial role has more prominence. US anti-trust policy has *defined* illegal practices and so a legal judiciary is appropriate, as opposed to the UK situation where *interpretation* of each situation is required and thus economic knowledge rather than legal expertise is the recipe required.

However the UK approach has its criticisms too, in that being case-by-case there are often inconsistencies in its findings. What all of the above systems have in common though is that they are resource sensitive; investigation into each case can take months or even years and call-upon huge quantities of both financial and manpower resource.

A4.3 Position of the European Union

Member States, as we shall see in the case of the UK later, have their own authorities to enforce national competition laws. However, since the introduction of the Single Market, it has become necessary to police the new marketplace to ensure its benefits reach all consumers within it – a task undertaken by the Commission.

The legal supervision of the Commissions actions belongs to the European Court of Justice and the Court of First Instance, which deals with actions brought against the Unions institutions over competition rules and other issues.

In addition to cartel monitoring, the Commission is also interested in dominant positions of firms (and abuses of such a position); mergers and take-overs (establishing if they will lead to a dominant position); the use of state aids and policies that threaten inter-State competition in trade; and the financing of state undertakings.

The legal framework for competition rules are set out in Articles 37, 85-94 of the Treaty of the European Union and Articles 4, 65-67 of the European Coal and Steel Community Treaty.

The Commission, acting either on its own initiative or following complaints from member states, companies, or individuals conducts policy. Companies who may fall foul of the legislation can apply for a "negative clearance", which means that after scrutiny the Commission will not take action, or an "exemption" which permits a restrictive agreement on the grounds that it offers substantial public benefits.

In terms of power, the Commission can visit companies without warning and demand access to documents, hold hearings with the companies concerned before giving a verdict, and, where anti-competitive behaviour has been established, impose fines. Competition law under the EU takes precedence over any national law within member states, as it is directly applicable to them.

As identified above, there is the facility to waive fines under the EU laws. In December 1996, this was amended, by the setting out of the circumstances in which such fines will be reduced or waived in cartel cases. The amount by which the fines can be reduced is now quantified in percentage terms of up to 10% of annual turnover.

In the past the Commission have dealt out substantial fines, but express concern that firms continue to engage in cartel activity. By reducing the fines, the Commission hopes to uncover further evidence of cartels and ultimately to stamp out such behaviour – perhaps a little optimistic?

- In order for the firms to be exempt (full or in part) from the fine, the following conditions must be satisfied:
- The enterprise must be the first to provide decisive evidence of the cartel's existence;
- It must terminate its involvement in the illegal activity before or at the time at which it informs the Commission of the existence of the cartel;
- It must provide the Commission with all relevant information and documentary evidence and continue to co-operate with the Commission throughout its investigation;
- It must not have compelled another enterprise to take part in the cartel and must not have instigated or played a key role in the cartel.

A4.4 Modes of Action

UK
Judgement is passed through the Restrictive Practices Court. It can issue an order that forbids the companies concerned to operate either that agreement in its original form, or another agreement to like effect. There is no specific *ex-post* monitoring of sectors or industries where agreements have been struck down to make sure that competitive behaviour results.

EU
The Commission can terminate an agreement found to be prohibited under Article 85 by issuing a formal decision that legally enforces abandonment of the agreement and can impose substantial fines on the firms involved.

US
The Federal Trade Commission issues a 'cease-and-desist' order – an injunction to the companies concerned to abandon those practices which have been found to be against the law. The penalties imposed depend on whether the case is a civil or criminal one.

Criminal penalties include the payment of fines and the imprisonment of offending businessmen, although in practice this latter sanction is rarely used.

ANNEX 5 DOWNSIZING & RETRENCHMENT

A5.1 Overview

Public Sector downsizing is becoming an increasingly significant part of economic development in developing countries. The premise here is the inefficiency resulting from overstaffing and the consequent need to reduce or downsize operations. Inevitably this implies some element of retrenchment (redundancy), which demands examination of the best way of estimating redundancy figures and also the best way to implement and evaluate the changes.

An important additional consideration for any party implementing such measures is the cost and measurement of compensation payments, and therefore how to reduce the 'cost' of downsizing'.

In 1996 the World Bank, through the Operations Policy Committee, began examining such issues. In short, it viewed that retrenchment should be estimated on the basis of shadow prices of labour as opposed to actual labour costs, with labour economics being used to predict the losses workers may experience as a result of being made redundant. It recommends using these losses in conjunction with the 'observable characteristics' of workers (such as age, education, experience) in order to help determine redundancy payments.

One of the main problems foreseen relatesd to the how to ensure that the best workers remain in employment, whilst the least effective members leave. One method employed as an incentive is the principal-agent approach whereby self-selection mechanisms highlight cases where productivity is not observable in the public sector.

But these methods may not be so easy to deploy in practice as the sheer scale of downsizing requirements in developing countries may be politically impossible. Thus the World Bank recommends that a voluntary approach be used with assistance to governments from multilateral organisations and donor countries. Severance pay is used to overcome worker resistance by providing them with an incentive to quit. But this is an extremely costly way of doing things, with average compensation and retraining packages amounting to several thousand dollars per worker (huge in developing country terms). This problem forced the Bank to modify its operational rules in 1996 to allow lending to fund severance pay. This now brings us on to how one should deal with the process of downsizing and therefore the considerable risk of it being mishandled.

A5.2 Problems with downsizing operations

A major issue is whether severance pay packages really will encourage the low productivity worker to depart or rather that it will induce the more productive worker to do so instead. The Bank sees the operation of downsizing in the same vein as any other investment project and thus subjects them to the same kind of evaluation. Problems are met however in that the connections between the financial and economic returns to be derived from downsizing operations are very tenuous.

Financial returns are reflected in the reduction of the wage bill, with positive returns indicated by the present value of the reduction being higher than the 'up-front costs' of the project – i.e. severance pay, retraining programmes, etc. Economic returns are seen through the better, more efficient allocation of labour across sectors, with positive returns indicated when displaced workers add more output or welfare when they are outside the public sector than when they were in it. More commonly, financial returns may be a poor indicator of economic returns.

As to the poor handling of such an operation, the Bank states that this is indicated by extensive rehiring of displaced workers by the same agency or enterprise. It indicates, in the best case, that some of the best workers were mistakenly considered redundant. In the worst case, says the Bank, it indicates that workers who had no intention of permanently leaving the public sector were able to cash-in by accepting "golden handshakes". Labour misallocation is believed to be shown by the retaining of low productivity workers.

The Bank study, by Haltwinger and Singh (1997), showed that rehiring was observed in 40 percent of the operations, and was very substantial in 20 percent of them. It suggests, therefore, that the economic returns to downsizing have been low.

In practice there are identification problems in relation to the productivity of workers, especially with poorer workers. This is due to the many other inefficiencies associated with public structures, such as pay scales. Here benefits come from subsidies and transfers from the budget which are financed by distortionary taxes. In addition, the Bank states that mass displacement of public sector employees may also affect the jobs and earnings of other workers. So tackling only one distortion cannot guarantee an improvement in economic efficiency.

Changing pay scales or achieving full cost recovery may not be possible for many governments, so a second-best approach is therefore needed through the use of a "shadow wage". The Bank states that workers whose productivity is lower than this wage should be considered redundant, and vice versa. Shadow wage formulas are found in the Bank report by Rama (1997). However, this approach does not work in situations where individual productivity is difficult to measure and so an alternative method is needed.

The Bank promotes that a percentage of redundant workers are produced by comparing the actual employment level to some supposedly optimal benchmark in terms of economic efficiency. Severance pay is offered to those willing to resign their public sector job voluntarily. The problem is that the percentage of those accepting the buyout may differ from the percentage of redundant workers. In addition the harder worker may be the first to leave as they would experience a smaller welfare loss than the lazy ones if they left the public sector. To prevent this agencies could offer those who relinquished tenure the chance to switch to better-paid fixed-term contracts – appealing to the harder worker more than the lazy one.

In practice, the Bank promotes a 'menu of options' that is not precise, but uses self-selection as a substitute for perfect information about the characteristics of public sector workers.

Where public sector workers cannot be legally dismissed, compensation that falls short of each workers perceived loss will fail to encourage their voluntary departure. There can be conflict in supporting efforts to tilt the budgetary process in favour of the poor and lending generous amounts of money to finance severance pay packages for public sector workers, who usually are not poor. Studies show that a better tailoring of severance pay offers could reduce the total cost of downsizing by 20 percent or more (Assaad, 1997).

A5.3 Size and scope of retrenchment in Africa

Although the exact number of employees retrenched is not known, it is estimated that between 2.5 and 3 million persons may have been affected. The first schemes were introduced in Africa during the mid-1980s with a target of cutting employee numbers by between 15 and 25 percent, but there appeared to be no rationale for such figures (BICC).
Despite the resistance of governments to undertake what they perceive to be politically risky measures, retrenchment has taken place in several countries.

GHANA: PUBLIC SECTOR EMPLOYMENT AND RETRENCHMENT, 1987 & 1992

GROUP	1987		1992	
	Numbers	% of total public sector	Numbers	% of total public sector
1. Core Civil Service	131 089	20.1	102 173	17.2
2. Education Services	159 000	24.4	167 370	28.1
3. Subvented Organisations	81 574	12.5	69 574	11.7
4. Security Organisations	29 000	4.5	29 000	4.9
5. Total Government Services	400 663	61.6	368 117	61.9
6. Net Retrenchment (1987-1992)	-	-	32 546	8.1
7. Public Enterprises	250 000	38.4	227 000	38.1
8. Net Retrenchment (1987-1992)	-	-	23 000	9.2
9. Total Public Sector (line 5 + line 7)	650 663	100	595 117	100
10. Net Retrenchment (1987-1992)	-	-	55 546	8.5

Source: Lecchor, 1994, p.164.

SENEGAL: CIVIL SERVICE VOLUNTARY DEPARTURE PROGRAMME, 1991

			ACTUAL FIGURES AS OF OCTOBER 1991		
Category/type of departure	Target number	Applications (number)	Number of actual departures	Share of total (%)	Average cost of CFA (Franc millions)
Voluntary Departure	2 850	2 458	2 155	57.5	4.8
Early Retirement	1 450	1 682	1 590	42.5	3.3
Privatisation	5 609	-	-	-	-
TOTAL		4 140	3 745	100.0	4.2
Departure by Grade:					
A (highest)		492	434	11.6	5.9
B		1 088	925	24.7	5.9
C		744	674	18.0	4.1
D		1 417	1 339	35.8	3.1
E (lowest)		399	373	10.0	2.2
		3 745	3 745	100.0	4.2

Source: Rouis, 1994, p.323.

In Gambia, following a census and staff audit, approximately 3,800 government employees (including 2,900 temporary employees) were dismissed. And in the Central African Republic between 350 and 400 civil servants have been removed so far, with more reductions planned for subsequent years (Nunberg & Nellis, 1995, p.19).

Approaches to retrenchment in Sub-Saharan Africa

Nunberg and Nellis (1995) list the following cost and employment containment measures in increasing order of perceived political risk:

1. Removal of 'ghost' or non-existent names and workers from the government payroll.
2. Elimination of officially sanctioned posts that are not currently filled.
3. Retrenchment of temporary or seasonal workers.
4. Enforcement of retirement age.
5. Freezing of recruitment.

6. Elimination of guaranteed entry to the civil service from the educational or training system.

7. Suspension of automatic advancement.

8. 'Voluntary' incentives – induced retirement of surplus workers.

9. Containment of wages (restraints or freezes).

10. Dismissal of serving civil servants.

It is also vitally important for any scheme that a detailed and comprehensive impact assessment programme is implemented. The following elements must be considered within this.

Employment costs
Available evidence points to the conclusion that results of the impact of retrenchment have been, at best, mixed. Initial numbers contained many 'ghosts' or 'phantom employees', and also governments found it difficult to sustain retrenchments due to 'revolving door' practices. In the short-run though, available evidence shows that countries have made some progress in reducing their wages and salaries as a share of GDP and current expenditure.

WAGE TRENDS FOR SELECTED GOVERNMENTS

COUNTRY	1980	1988
Central African Republic (CAR) (1982)		
Wages & Salaries (billions CFAF)	23.7	25.4
W&S/current expenditure %	65.1	58.2
Gambia		
Wages & Salaries (000 Dalarie)	52 775	78 387
W&S/current expenditure %	40.7	19.3
Ghana (1981)		
Wages & Salaries (millions of Cedis)	1 257	49 464
W&S/current expenditure %	-	44.6
Guinea-Bissau		
Wages & Salaries (% of GDP)	16.0	5.3
W&S/current expenditure %	59.5	29.4
Senegal		
Wages & Salaries (billions of CFAF)	78.3	125.1
W&S/current expenditure %	61.7	50.4

Source: Nunberg and Nellis. 1995. Table 7, pp.31-35.

5.3.1.1 SEVERANCE PAYMENTS FOR SELECTED COUNTRIES

COUNTRY	PAYMENTS
Central African Republic	40 months salary and the employees accumulated pension fund contribution
Gambia	1.2 months salary per year of full-time service. One month for non-permanent staff
Ghana	Four months basic salary, plus tow months basic salary per year of full-time service
Guinea	Flat amount equal to about five years basic salary for the average worker, with 30% paid up front and the balance paid in monthly instalments for the voluntary departure programme
Guinea-Bissau	One years salary paid in monthly instalments
Senegal	Up to 48 months salary; 60 months for the two lowest grades. No unilateral firing of civil servants
Uganda	3 months basic salary in lieu of notice, one months salary in lieu of leave entitlement, transport money from place of work to home district headquarters. Severance package equivalent to 3 month's basic salary for each completed year of pensionable service, up to maximum of 20 years. Non-permanent employees received one month's basic salary in lieu of leave entitlement plus transport to home village. Voluntary retiree received an extra "golden handshake" of UShs. 1 million (1,000 US$)

Labour Markets

Most retrenchments concentrated on the unskilled and semi-skilled workers. Since these are in large numbers, it would be expected that retrenchees from the public sector would depress wages as they compete with others in the private sector for available jobs. But it is also possible that many low-level employees move freely between the formal and informal sectors and retrenchment would simply push them out of formal sector employment.

A5.3.2 Gender

It is commonly believed that structural adjustment in general (Goetz, 1995) and public sector reform in particular (Nzomo, 1995) have detrimental effects on women and other vulnerable groups in the adjusting countries. Available evidence seems to support this claim. A World Bank study of labour markets in several African adjusting countries, Horton *et al* (1991) found that women suffered more because they are:

- More concentrated in the informal sector which tended to absorb excess labour
- Predominantly in food crop agriculture, whereas resources have tended to go to cash crops
- Less educated, and therefore less competitive in the labour market
- Less attached to the formal sector labour market, and therefore more likely to leave either voluntarily or with minimal pressure

- More concentrated in the lower level jobs which suffered from retrenchment proportionately more than other job types
- Less attractive and competitive in the private sector than men.

In addition to what has been discussed above, the reformer must also consider elements that relate to demobilisation, and they include the following.

A5.3.3 Policy Objectives

There is a need to develop shared understanding and acceptance of programme policy objectives and their immediate and long-term implications. Donors generally saw retrenchment as a means of cost containment, improving institutional performance and good governance, whereas recipient governments were more concerned with hedging political risks, maximising donor support, and finding alternative employment for retrenchees.

BICC believe that donors, governments, opposition parties, as well as civil society need to develop a consensus as to the key objectives, implementation, modalities, and realistic expectations from demobilisation at the macro, meso and micro levels. A workshop which includes stakeholder analysis might help to bring this about (Kiggundu, 1996b).

A5.3.4 Political Risk Analysis

Governments of adjusting countries have often associated reform with danger involving political risks (e.g. riots, coups), administrative resistance (e.g. strikes), or economic sabotage (e.g. smuggling). Civilian reforms, on the whole, do tend to be less politically risky. Initiatives must be taken to develop local and national capacities and institutions to manage the changing risks of demobilisation as the country evolves from a state of war (Somalia) to absence of war (Mozambique), peacemaking (South Africa), and democratic development (Namibia).

A5.3.5 Lack of Data and Objective Information

Public sector reform in Africa is characterised by a generalised lack of reliable data and objective information.

Other important issues relate to social implications, and human resource development and utilisation. This has certain policy implications, the following of which are listed by BICC:

1. Importance of a clear policy objective and the means by which they are to be achieved.
2. The need to take a long-term perspective, not only because reforms take time, but also because short-term initiatives tend to waste resources with little or no long-term benefits.
3. Assessment and development of local capacity for effective programme implementation is critical. Sustaining these initiatives requires local political, institutional, and administrative support and capacities.
4. Need for more emphasis on reintegration and human capital development and utilisation rather than simply getting rid of people with little or nothing to do.

5. Experience shows that while the costs of implementing these programmes are high, the long-term benefits are not so obvious.
6. It is important to realise that these programmes are likely to have differential effects on various sector or subgroups. It is important to have well-defined measurement and evaluation strategies including, wherever possible, baseline data, tracer studies, and multi-country comparative case studies.
7. Alternatives to public sector employment should be studied rather than assumed.
8. The role of the state in the development and effective utilisation of human capital may be redefined but should not be assumed non-existent.
9. Activities such as retraining, redeployment, credit, public works, and personnel databases should not be undertaken for symbolic or political reasons where they have been shown to have limited practical effects or where they are administratively difficult.
10. Governments must do proper homework before, during and after the formulation and implementation of these programmes. There are no blueprints, therefore local knowledge and experience is very important.

Operational implications are also considered by BCCI, who believe them to include the following:

1. The process and modalities of implementation are important: participation, understanding, ownership, commitment, timing, sequencing, experimentation, etc.
2. There is a need to think through the issues and to develop strategies for overcoming individual and institutional resistance and impediments to effective programme implementation. Institutional and stakeholder analysis may be necessary.
3. Dispersed and unorganised retrenchees may be powerless and vulnerable. In the absence of strong trade union representation, efforts to organise them through civil society organisations (such as NGO's) may be encouraged.
4. There is no conclusive evidence as to the most effective way of packaging and delivering benefits (e.g. cash, materials, training, etc.) to the departing employees. Experimentation and sharing of experiences may be the best way to proceed.
5. Others outside the central government including local government, the private sector, family and tribal leaders, church organisations, etc. should be consulted and invited to participate in the formulation, implementation, monitoring and evaluation of these and other redeployment programmes.

ANNEX 6 BUYING-OUT CAPACITY

A problem closely connected to that of monopoly and cartels is that of buying-out capacity. This action refers to the decision to purchase market share from a dominant firm so as to (in effect) gain control of supply of the product. Perhaps the best way of explaining this is through an example; with the Common Fisheries Policy of the EU being a good example.

This method is very costly and can, in practice, be extremely hard to enforce and obtain the necessary political agreement. It is reasonable to consider this topic in connection with downsizing and retrenchment. Buying-out capacity can be seen as a method of downsizing. But there are many complex forms of this, and the process, as ever, is never simple.

The main purpose of including this review demonstrate how buying out capacity has taken place and it shows that it is possible to reduce the size and scope of an industry (even contentious ones such as fisheries - and perhaps therefore transport). But this is only as long as there are sufficient instruments and that policy is regularly reviewed and adapted.

A6.1 EU Common Fisheries Policy (CFP)

Fishing contributes a relatively small amount to Member State economies (often less than 1%), but it represents an industry that many local communities depend on and is one of great contention. The policy relates not only to fishing boats but all connected industries, and so one of the problems for the policy maker is the indirect consequences of changes that they make – the externalities of change.

The need for CFP, according to the EU, came about from evidence of dwindling stocks and concerns about environmental impact. Agreement was not concluded until after talks began in 1973, and even then it was on the basis of a 20-year term and did not allow free access to all fishing grounds. The conservation and management of resources was reviewed in 1992 with identification of the need for a rational, responsible and sustainable exploitation of fisheries, a more effective control of the whole fishing industry, and a broad sharing of responsibilities for managing the CFP. These recommendations resulted in new basic regulation and new control regulation, with the aim of ensuring greater coherence between different aspects of policy, and to remove the partition that had divided the CFP from other Community activities. They were also designed to take account of the profound changes affecting the sector due to the serious imbalance between the number of boats and quantities of fish available.

Financial measures have been adapted too that allow the fishing industry to bear the social and economic consequences of the necessary restructuring of the fisheries sector.

A6.1.1 CFP Operation

The main contentious issue relates to the location of fish stocks and who is allowed to fish there. The instruments developed are in the form of licences and permits, providing for a management mechanism to limit the fishing effort of individual vessels having access to certain fisheries. There are also a variety of technical measures (net, catch sizes etc) that are employed, but the concept of Total Allowable Catch (TAC) is the key management tool to limit stock exploitation rates. Based on scientific advice, these rates are studied and then limits are imposed based on the results. TAC levels are fixed by the Council of Ministers, each TAC being divided up among the Member States in the form of the quotas. These are then allocated nationally or exchanged with other Member States. In 1995 the "fishing effort regime" was introduced to establish a link between the captures and the fishing capacity of the fleet.

A6.1.2 Monitoring

Policing and enforcement is the responsibility of Member State governments, with effectiveness being monitored by a small team of the Union's own inspectors. In 1993 the powers of the controls were strengthened and extended to cover all fishing activities, and penalties being decided by national courts. This shows the importance of adapting policy when loopholes and flaws have been identified.

Penalties can range from hefty fines, confiscation of fishing nets, or fish caught and even of the boat itself to temporary suspension or permanent withdrawal of fishing licences. The Union provides financial aid to Member States for measures to strengthen control and for purchasing fishery protection vessels and aircraft.

A6.1.3 Common organisation of the market

Measures that have been/are introduced are designed to stabilise the market, guarantee a steady supply of quality products, ensure reasonable prices for consumers, and to support fishermen's incomes. The key elements of the market organisation are:

- Quality standards covering size, weight, presentation, packaging and labelling.
- A comprehensive pricing system which allows prices to be fixed by supply and demand but which sets a floor price at which fish are withdrawn from the market and not sold. In most years, the total quantities are quite small – less than 50,000 tonnes.
- Producers organisations, to which most fishermen belong market the fish, help to improve quality levels, adjust supply to demand and make sure that most fishing quotas are properly managed.
- Imports without which the Union could not satisfy domestic demand for fish. After fruit and vegetables, fish is the Union's second largest food import. Prices are monitored by the Commission, which intervenes whenever imports undermine the market.

Lessons can be learned from here too. The importance of setting standards for the product is highlighted, as is a structured pricing system. An interesting method employed relates to the fishermen's 'Union' that is responsible for adjusting itself to market conditions and is responsible for marketing its own product. Attention is also given to external influences, which in the form of vehicle price differentials, can be a problematic application to the transport sector.

A6.1.4 Third Countries Agreements and International Conventions

This is an essential element of the legislation and the policy, providing access for the Union's fleet to the waters of non-member countries. Without this it is clear to see the possible resulting substantial reduction in fishing opportunities, with serious repercussions for Community fishermen.

The arrangements are particularly useful in reducing the fishing effort in those waters, given the surplus capacity in EU waters. There have been approximately 26 concluded agreements with various types of concession offered, including:

- Reciprocal arrangements
- Access to surplus stocks
- Access to stocks in return for market access
- Access to stocks in return for financial compensation
- Access to stocks in return for payment and market access.

A6.1.5 Structural policies

It is important here that one identifies the instruments developed and used for dealing with structural problems, with an aim of establishing a more secure and stable future for the industry:

- Multi-annual guidance programmes (MGP) – aimed at restructuring and modernising fishing fleets by fixing ceilings for the fishing effort by the main segments of the fleet.

- The financial instrument for fisheries guidance (FIFG) is a fund available to all involved in the industry that can contribute to measures including the permanent withdrawal of vessels, fleet renewal and modernisation, and investment in aqua-culture, development of coastal waters, port facilities, processing, and marketing. The FIFG budget for 1994-1999 is ECU 2.7 billion.

- Socio-economic measures are employed in areas where fishing can benefit from aid from the European Regional Development Fund (ERDF) and the European Social Fund (ESF). ERDF focuses on stimulating stable, productive and job-creating economic activities while the ESF assists in vocational training and retraining, adult education, and incentives to recruit newly created jobs.

- The PESCA Community Initiative seeks to generate clearly focused projects to help the fishing sector to adapt and coastal areas to diversify their economic activities.

The EU also attach importance to considering how a policy will be applied in the future, so it follows that such considerations should be built into any policy. So how does the EU view the future of the CFP?

A6.1.6 The future of CFP

In its vision for what needs to be addressed in the future, the EU views the following factors as important. They are, balancing fishing capacities and resources, establishing a management and conservation policy (Mediterranean), the impact of fishing on the environment, and also methods of adapting the sector to the international context. Methods by which all of this can be achieved are detailed by the EU, but are at various stages of development.

The fourth Multi-annual Guidance Programmes to adjust fishing effort (1997-1999) are said to be designed to ensure better integration between resource conservation and the structural aspect of the CFP. It will take into account the interest of the industry, and all the parties involved will be consulted. It has been decided that a specific adjustment programme will be drawn for each fleet, which will be backed up at the implementation stage by aid granted from the FIFG.

The Council has also moved for greater uniformity through regulation, establishing conditions governing the use and prohibition of certain equipment, with minimum net and landing sizes. This is all done with a view to co-operation with all surrounding countries. The EU views sustainable and rational management if fishery resources as a major preoccupation.

In terms of further future developments, it feels the industry should be prepared for international development, in particular in terms of commercial policies and relations with third countries.

It states that arrangements to be concluded in the future must be adapted to the political and/or legal changes and to the expectations of each partner, incorporating the special socio-economic features of each country and aiming to establish the most consistent partnership in the long-term. In the framework of the internal market and the commercial policy, the efforts to be made in coming years must be geared to achieving equilibrium between the supply needs of the processing industry and the interests of the Community production in competitive conditions.