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DIALOGUE

PPPs: Public Costs and Risks for Private Profits

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Abstract After the generally acknowledged failure of privatization, public–private partnerships (PPPs) have been promoted as a better means for private interests to secure lucrative rents at public expense. PPPs are supposed to reduce the fiscal burden, fill the resource gap for much needed investment to achieve economic development and to better provide infrastructure and services. These claims are grossly exaggerated in light of actual experience. The private sector, for example, is supposed to be better in risk assessment and management; but all too often, the public sector ends up bearing the bulk of the risk, worsening fiscal burdens contrary to what has been promised. Through revenue guarantees to the private partner, PPPs socialize risks, enabling private gains. PPPs in social sectors, such as health, are particularly problematic as they tend to adversely affect access, thus undermining universal health coverage. PPPs have also distorted national investment and development strategies. Thus, by and large, PPPs generally do not serve the public interest well. Hence, public alternatives, including procurement, have to be considered, before governments commit to PPPs. Instead of promoting PPPs, such as 'blended finance' arrangements for aid delivery, sincere development partners should empower governments through appropriate strategic capacity building and budget support.

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The widely acknowledged failure of most privatizations in advancing the public interest has forced governments to retreat from continuing to pursue this disastrous policy. Instead, the preferred policy approach for the last two decades has been public–private partnerships (PPPs). Instead of replacing governments, private corporations are using governments through PPPs to promote their own interests.

PPPs in the form of 'blended finance', export financing, and new aid arrangements have, in fact, become effective means for donor governments to support their corporations' bids for PPP contracts in developing countries. They often involve public financing for developing countries to 'sweeten' a bid from an influential private company from the donor or creditor country concerned (Talbot 2015; Kostyak et al. 2017). Such business support arrangements are increasingly passed off and counted as overseas development assistance (ODA) (Oxfam 2017; Pereira 2017).

PPP Advantages Exaggerated

PPPs typically involve long-term contracts, underwritten by government guarantees, with which the private sector builds (and sometimes operates) major infrastructure projects or services traditionally provided by the state, such as hospitals, schools, roads, railways, water, sanitation and energy. PPPs have been promoted by many OECD governments, and some multilateral development banks—especially the World Bank—as the best solution to the

shortfall in financing needed to achieve economic development including the Sustainable Development Goals (SDGs).

Since the late 1990s, many countries have embraced PPPs in various diverse areas, ranging from healthcare and education to transport and infrastructure—with many problematic, albeit generally long term and under-acknowledged consequences. PPPs have been less common in developing countries, especially poor ones, but that too is changing rapidly, with many countries in Asia, Latin America and Africa now passing enabling legislation and initiating PPP projects. Thus, the recent period has seen growing advocacy of and enthusiasm for PPPs, although experiences with PPPs have been largely, but not always negative, with few PPPs delivering the best results in the public interest.[1]

Nevertheless, the recent surge in developing country interest in PPPs is understandable. Short of adequate fiscal and aid resources, most developing country governments cannot finance needed investments alone. The UN Intergovernmental Committee of Experts on Sustainable Development Financing estimated in 2014 that annual global savings (both public and private sources) were around US$22 trillion, when global financial assets were around US$218 trillion.[2] Thus, the third International Financing for Development (FfD) Conference in Addis Ababa in mid-2015 recommended 'blended finance' as well as other PPPs to pool public and private resources and expertise to achieve the SDGs.

Yet, PPPs have a poor record of filling infrastructure shortfalls, being cost-effective and ensuring access and equity, undermining the SDGs' principle of 'leaving no one behind', including the promise of universal health care. Government partnerships with for-profit private entities have resulted in worse fiscal outcomes, in terms of both finance and value for money.

Misleading claims have been used to justify PPPs. They typically overcome budgetary constraints by taking expenditures and related debt off-budget via government guaranteed debt which burden future governments, consumers and taxpayers. Macroeconomic problems arise due to PPP failures, poor investments and the build-up of sovereign debt liabilities, albeit for government guaranteed rather than government debt per se. A fundamental problem involves risk sharing, not only of related costs, but also ensuring sufficient future revenue streams (Ahmed et al. 2014).

[1] For an earlier summary of trends in PPPs and some issues involved, Jomo et al. (2015), Ahmad et al. (2014).

[2] Report of the Intergovernmental Committee of Experts on Sustainable Development Financing—Final Draft, 8 August 2014. https://sustainabledevelopment.un.org/content/documents/4588FINALREPORTICESDF.pdf

Driven by profit considerations and political priorities, rather than genuine economic considerations, PPPs typically incur more debt, risk and transactions costs than government services and procurement, especially in the health sector.[3] Neither PPP hospital building quality nor facilities management services have delivered better value for money. Thus, underfunding and higher PPP costs inevitably result in services cuts to reduce deficits.

PPPs More Expensive

PPPs are, in many cases, the most—not least—expensive financing option. They cost governments—and citizens—significantly more in the long run than if projects were directly financed with fiscal resources. But PPPs are attractive to politicians and others because they can be hidden 'off balance sheet' as they do not show up in government budget and debt figures, giving the illusion of 'free money' to politicians.

Shifting from sovereign debt to government guaranteed debt does not reduce, but rather, tends to obscure and hence accelerate increasing overall public sector debt liabilities. PPPs often obscure and weaken accountability as project and other related debt are taken 'off-budget', and hence, are no longer subject to parliamentary, let alone public scrutiny.

Thus, despite claims to the contrary, PPPs are often riskier for governments than for the private companies involved; typically, the government is expected, if not contractually required to step into assume costs if things go wrong. That is, PPPs typically socialize costs and risks while guaranteeing profits for the private partner.

Some longer-term fiscal implications of PPP-related 'contingent liabilities' have been acknowledged by the IMF, another advocate of PPPs. Recognizing the problem, both the World Bank and the OECD have developed PPP guidelines for governments.

PPPs can provide attractive financing arrangements, e.g., due to low interest rates thanks to 'risk-free' government guarantees. Nevertheless, private finance still accounts for a small share of infrastructure financing all over the world. In any case, concessional financing arrangements cannot improve a poor project although they may reduce its financial burden.

Arguably, there has been some success with infrastructure PPPs, but these appear to have been largely due to foreign government enabled financing arrangements. In contrast, PPPs for social services, e.g., for hospitals and schools, have generally delivered much poorer results compared to some infrastructure projects.

[3] For a summary of research findings, Torchia et al. (2015).

Hence, in most cases, PPPs are the most expensive financing option, and hardly cost-effective compared to good government procurement. They cost governments—and citizens—significantly more in the long run than if the projects had been directly financed with fiscal resources, including government borrowings. In sum, PPPs can incur not only higher financial costs, but also generate modest, if any efficiency gains as there is nothing inherent in most PPPs to ensure them.

Marginalizing Public Interest

PPP contracts are typically complex. Negotiations are subject to commercial confidentiality, making it hard for parliamentarians, let alone civil society, to scrutinize them. This lack of transparency significantly increases the likelihood of abuse and undermines parliamentary and democratic accountability.[4]

PPPs also undermine democracy and national sovereignty, not only because contracts tend to be opaque, but also are often subject to unaccountable private international adjudication—rather than national or international courts—due to investor-state dispute settlement (ISDS) commitments. Under World Bank-proposed PPP contracts, for example, national governments can even be held liable for losses due to strikes by workers.

PPPs tend to exacerbate inequality by enriching politically well-connected businesses who profit from such projects, thus accumulating even more wealth at the expense of others. The more governments pay for such purposes, the less they have to spend on social services, including universal healthcare and social protection.

A research report for the UK Department for International Development found 'a considerable and growing body of evidence which suggests that the greater portion of the public money spent on such partnerships produces, at best, no significant effect on the urban poor. At worst, much of the expenditure may actually lead to increased poverty by diverting public money and energies away from service delivery, subsidizing corporate profits, and increasing social exclusion'.[5]

PPP contracts often undermine consumer, citizen and human rights, and the state's obligation to regulate and provide in the public interest. PPPs often increase fees or user charges for services, and may limit government capacity to enact, implement and enforce new policies—e.g., strengthened environmental or social regulations—that might affect particular projects.

PPPs have become an increasingly popular way to finance 'mega-infrastructure projects'. But poorly designed and supervised dams, highways, pipelines, energy or transport infrastructure and plantations can ruin habitats, displace communities and devastate natural resources. Typically, social and environmental legislation has been weakened to create more attractive business environments for PPPs.

PPPs have thus often led to forced displacement, repression and other abuses, especially of protestors, local communities, indigenous peoples, natural resources and environments. Not surprisingly then, 'dirty' PPPs, exacerbating environmental destruction, undermining progressive environmental conservation efforts and worsening climate change, have been increasing.

Perverted Priorities

In 67 low- and middle-income countries, achieving SDG 3—healthy lives and well-being for all, at all ages—is expected to require new investments, increasing over time from an initial US$134 billion annually to US$371 billion yearly by 2030.

DEVEX, a private-sector driven network of development 'experts', misleadingly claims that PPPs can unlock billions for health financing. It does so by citing some undoubted philanthropic partnership success stories—such as the Global Alliance for Vaccine Initiatives (GAVI) and the Global Fund to Fight Aids, TB and Malaria—to claim that national PPPs will have similar success.

However, systematic reviews of research findings suggest a much bleaker reality (Roehrich et al. 2014; Torchia et al. 2015; Kostyak et al. 2017). In low- and middle-income countries, healthcare PPPs have increased competition for funding, inefficiencies and waste. Meanwhile, PPP terms favour private partners, undermine national health policy goals and worsen government negotiating capacity vis-à-vis powerful foreign healthcare companies.

Meanwhile, influential private partners have reshaped government priorities and national health policies to better serve commercial interests. It is also well known that despite considerable rhetoric to the contrary, donor-funded PPPs are typically unsustainable, and inadvertently undermine national health strategies, policies, capacities and capabilities besides Agenda 2030.

[4] Hodge (2006: 318) argues, 'whilst partnership notions have a long historical pedigree, the new long-term contractual form of partnership has three characteristics that deserve research: the preferential use of private finance, high level of complexity through bundled contracts, and new accountability and governance assumptions. Moreover, the first two of these characteristics have major implications for the third.' Drawing on the research literature as well as parliamentary inquiries, he concludes that 'the PPP tool currently lacks legitimacy in the eyes of citizens in whose name it is being employed'.

[5] Cashdan (1998). Oxfam (2014) warned that large-scale partnerships with the private sector could undermine Africans' land rights, exacerbate inequality and damage the environment.

PPPs often divert domestic resources from national priorities, thus undermining public health. Such redirection typically exacerbates health disparities, adversely affecting vulnerable groups. Health workers often prefer to work for better funded foreign programmes, undermining the public sector.

Thus, PPPs inadvertently encourage governments to abdicate their responsibilities for promoting and protecting citizens' health. Partnership arrangements with the private sector are neither subject to public oversight nor transparent, creating more scope for corruption. While PPPs can undoubtedly mobilize private finance, this can be done at lower cost via government borrowing.

A managed equipment services PPP with GE Healthcare in Kenya, often cited as a success story, has actually undermined Kenya's health system, providing inappropriate training and diverting scarce fiscal resources. Consequent non-payment of salaries to government health employees has encouraged emigration of well-trained health professionals to rich countries, worsening the Kenyan situation.[6]

Alternative Approaches

There is an urgent need to consider and develop alternative arrangements to PPPs as currently conceived and implemented. But, in recent decades, so-called free trade agreements and investment treaties have been eroding the rights of governments to pursue such alternatives in the national interest.

Government procurement, using sovereign debt if necessary, has generally been much cheaper, contrary to misleading PPP advocacy. Generally, PPPs are much more expensive than government procurement despite typically subsidized credit. With a competent government or an accountable civil service or even capable consultants doing good work, efficient government procurement has generally proved to be far more cost-effective than PPP alternatives.

It is also important to establish under what circumstances efficiency or other gains are achieved, and when these are less likely to occur. It is crucial to make sure that PPPs are not abused, as the government or public sector, and ultimately, the public itself bears the costs and takes most of the risks, while most profits accrue to the private partner, not the public.

Many contemporary examples suggest that the public interest would be better served by transparent bidding. But many PPP proposals have been approved and implemented without any real or meaningful transparency or competition despite much pious rhetoric by donor governments, international financial institutions (IFIs) and multilateral development banks (MDBs) about the importance of and need for competition and transparency.

In a contemporary variant of previously denounced 'tied aid', developed country governments increasingly use their aid or ODA budgets to promote their supposed national interests, e.g., by providing 'blended finance' on concessional terms, or by otherwise advancing the interests of such businesses by securing PPP contracts. While old style 'tied aid' typically sought to export goods and services from the donor country, the recent and still growing trend actually promotes the interests of specific private corporations as in the donor's national interest.

Meanwhile, aid-receiving governments have been advised, encouraged or required to replace government procurement with PPP arrangements to undertake infrastructure and other projects despite their mixed, but generally poor records, even in the developed countries themselves. Hence, many developing countries have little choice but to deal with such active promotion of PPPs. As many developing country governments believe they cannot dodge the PPP bullet, they need to be able to better deal with them.

Thus, to secure financing for needed infrastructure, they need strong institutional capacity to create, manage and evaluate PPPs. Governments need to have the capacity to critically evaluate PPP proposals, and to make counter proposals when needed. It is therefore important for government institutional capacity to be enhanced to create, manage and evaluate PPP proposals.

Empowering Governments

Governments should be empowered, and thus discouraged from presuming that they have no choice but to accept PPP proposals from the private sector. Stronger institutional capacity to better cope with PPPs requires having a dedicated competent service committed to national and public priorities and concerns in order to do the needed. Hence, strengthening public sector capacities to cope with PPP proposals is necessary and urgent.

This is not a major problem in some emerging market economies, which generally have more choice in such matters, but it is for many poorer developing countries. Most low income and many middle income developing countries do not have the capacity, let alone the capabilities

[6] See the comments by Dr. Elly Nyaim, the Kenya Medical Association chair. https://www.nation.co.ke/lifestyle/dn2/Brand-new-equipment-same-old-problems-equipments/957860-2621846-gykocd/index.html.

needed to be able to effectively evaluate and respond to such proposals.

Hence, most developing countries need international technical support to accelerate capacity building. Using private consultants to fill the gap in the interim before national capacities are sufficiently developed is attractive and may be necessary in the short term, but it is often forgotten that most such consultants tend to be mainly oriented to serving 'better paymasters' from the private sector.

ODA should therefore enable public sector capacity building, rather than give governments little or no choice. Instead of helping countries develop such capacities, much ODA often gives developing country governments little choice but to accept some donor government-backed PPP proposal.

As many governments may not be able to develop such a capacity with the ability to deal with varied PPP proposals, one alternative is for them to work together to develop a shared capacity. But they currently have no choice but to rely on organizations committed to PPPs, such as MDBs or IFIs. But so far, these have largely failed to credibly provide such capacities. They have also not enabled, let alone encouraged cooperation among developing countries to better cope with the PPP challenge, partly due to their current inclination to promote and enable PPPs as directed by their major shareholders.

Internationally agreed guidelines could also help. But guidelines developed by the World Bank may not adequately safeguard developing country interests as it is beholden to developed country shareholders who are typically enthralled by their corporate interests. After all, the World Bank is hardly a neutral agent as it is engaged in promoting PPPs, especially through its International Finance Corporation (IFC).

Therefore, international guidelines for PPPs need to be developed multilaterally through an inclusive multi-stakeholder process, perhaps through the United Nations Financing for Development (FfD) process. Alternatively, the United Nations Conference on Trade and Development (UNCTAD) in Geneva is well placed to work on such guidelines which would go some way to levelling the playing field.

Such guidelines should enhance developing countries' bargaining and negotiating positions, e.g., by ensuring competition through open bidding. Such guidelines should also seek to minimize, if not avoid abuse of PPPs, including by ensuring that public money is not used to subsidize private costs, risk-reduction and rents. Responsible and accountable developed and developing country governments must work together to ensure that they are all better able to cope with growing donor state sponsorship of and support for private corporate expansion.

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