

IsDB



البنك الإسلامي للتنمية
Islamic Development Bank

PUBLIC PRIVATE PARTNERSHIP POLICY

Sustainable Economic and Social Development Through Infrastructure Development



Public-Private Partnership Division
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Abbreviations

10YS	Ten-Year Strategic Framework
ADF	Alternative Development Finance
CC	Climate Change
ESS	Environment and Social Safeguards
GVC	Global Value Chain
IBG	Infrastructure Business Group
ICT	Information and communication technology
ICIEC	Islamic Corporation for the Insurance of Investment and Export Credit
IPPs	Independent Power Projects
IsDB	Islamic Development Bank
MC	Member Country
MDB	Multilateral Development Bank
MTN	Medium-term note
P5P	President's Five-Year Program
PPP	Public-Private Partnership
PSE	Public Sector Enterprise
PSP	Private Sector Participation
RL	Reverse Linkage
RISE	Regional Infrastructure Supranational Enterprise
STI	Science, Technology & Innovation
SME	Small and Medium Sized Enterprises
SOE	State Owned Enterprise
UN	United Nations
VfM	Value for money
VGF	Viability Gap Funding

Purpose, Objective and Background

1. The public-private partnership (PPP) Policy of the Islamic Development Bank (IsDB) is prepared in the context of ongoing reforms and the strategic agenda driven by the President's Five-Year Program (P5P). This Policy will be implemented in line with IsDB's endorsement of the SDGs, and its thematic and sector policies.
2. The Policy will establish the direction for the IsDB's PPP interventions in MCs to create a conducive environment for mobilizing private capital for infrastructure development. It fulfils the need for guiding the Bank's PPP interventions. This Policy is consistent with IsDB's strategic priorities and is focused on ensuring synergies with other activities of IsDB. PPP is a key instrument to implement the corporate strategy as outlined in the Ten-Year Strategic Framework (10YS) and the President's P5P. Subsequently, a Strategy and Operational Plan will be developed to provide a methodology for implementation.
3. The Policy will enable streamlining of PPP operations as well as associated non-sovereign infrastructure financing operations, advisory and capacity building, resource mobilization, awareness creation, and promotion of Islamic finance for infrastructure development in MCs. The Policy focuses on increasing support to MCs and will be aligned with the unique contexts of MCs, ensuring IsDB's fullest support to their socio-economic development goals, policies and strategies.
4. IsDB is in consensus with MDBs and infrastructure investors about a significant funding gap to meet infrastructure needs. The gap is wider for low to medium-income MCs which rely on MDBs support and private sector to fill the funding gap.
5. The MCs span the range of economic development from highly developed countries with large economies, to emerging economies to 21 countries designated by the UN as least developed. Consistent among MCs is an infrastructure deficit that calls for increased financing from both private and public sectors. Yet there has not been an upward trend of private investment. In fact, infrastructure investments leveraging private sector participation have been inconsistent at best. The relatively minor role of the private sector in many MCs is a direct consequence of a weak enabling environment for private sector financing and PPPs, especially in less developed countries. This presents a need to scale up private sector investments.

6. An assessment of the PPP experience of IsDB MCs reveals three major trends:
 - i. **Limited enabling environment and institutional capacity:** many MCs are struggling to build an enabling environment or have not begun the process of setting up public institutions with capacity for developing PPPs. These limitations pose obstacles for the MCs to attract private investors.
 - ii. **Limits in project selection and preparation:** there is a lack of capacity in many MCs to identify infrastructure projects suitable for PPP, and a lack of financial and technical expertise to undertake feasibility studies and business case analysis for projects to proceed to the next stage.
 - iii. **Financing gap:** most MCs have limited means to prepare and procure PPP projects, which limits their ability to attract capital. It is imperative that the PPP eco-system be sufficiently developed, otherwise the flow of capital will move to economies offering better risk-return choices and MCs will continue to rely on MDBs with shrinking sovereign windows to finance infrastructure.

7. These trends point towards opportunities for IsDB intervention in PPP, in line with strategies and goals outlined in the IsDB's 10YS and the P5P, which show that PPP is a key instrument to implement the corporate strategy of IsDB:
 - i. **10YS** has three layers of focus: strategic objectives, strategic pillars, and guiding principles. The strategic pillars, based on IsDB's mandate, core strengths, capabilities and experience have five areas of commonality with PPP services to be provided by IsDB. These pillars are economic and social infrastructure, private sector development, inclusive social development, Islamic finance sector development, and capacity development.
 - ii. **P5P** calls for greater selectivity for future operations, considering the needs of MCs and guidance from best practices. Of the six actions in the P5P, PPP activities align with three: delivery, financing, and reinforcement.

8. The IsDB has the experience and capacity to support MCs in developing their PPP policies and programs in realization of infrastructure projects, as follows:
 - i. Firstly, the corporate strategy under the P5P program calls for gradually enhancing non-sovereign interventions and offering a clear role for PPP in engagement with, and support of, MCs.
 - ii. Secondly, the IsDB has supported the PPP enabling environment and capacity building, and used its own balance sheet and mobilized market resources to finance infrastructure in more than a third of its MCs. Since 2005, IsDB has provided over USD 4.5 billion to finance PPPs.

- iii. Thirdly, IsDB's Islamic financing and insurance complement the funding by other MDBs. IsDB is the only Islamic financing institution that co-exists with conventional lenders in providing long-term infrastructure finance, and mobilizes financial resources from the wider Islamic financial markets.

Figure 1: 33km LATAR Expressway in Malaysia; Co-financed by IsDB



Definitions

9. **PPP:** For the purposes of this Policy, PPP is defined as “a partnership between a public authority and the private sector for achieving jointly set goals through a long-term partnership contract which involves a risk-sharing approach and a performance-based payment to the private sector (either by the user or public authority)”.
10. This Policy will distinguish between social and economic infrastructure PPPs. **Social infrastructure PPPs** are broadly defined as the construction and maintenance of facilities that support social services such as healthcare, education, and public facilities. **Economic infrastructure PPPs** are defined as the construction and maintenance of facilities and services which benefit the process of production and distribution, such as irrigation, power, transport and communication.
11. **Enabling environment development** includes assisting in developing supportive PPP policies, legal and regulatory frameworks, and capacity building and institutional strengthening to ensure good governance and transparency in award and oversight of PPP concessions.
12. **Project preparation and procurement** includes PPP project identification, planning and value-for-money (VfM) analysis, feasibility studies, advising on project procurement and PPP concession in support of government institutions.
13. **Project implementation** includes financing and co-financing of PPP projects on behalf of the Concessionaire with a variety of products and tools, resource mobilization from the private debt market, implementation oversight and project monitoring over the life of the financing. This support is provided to the PPP concession and can be blended with specially arranged viability gap funding (VGF) in collaboration with IsDB's sovereign window of operations.

Policy Scope

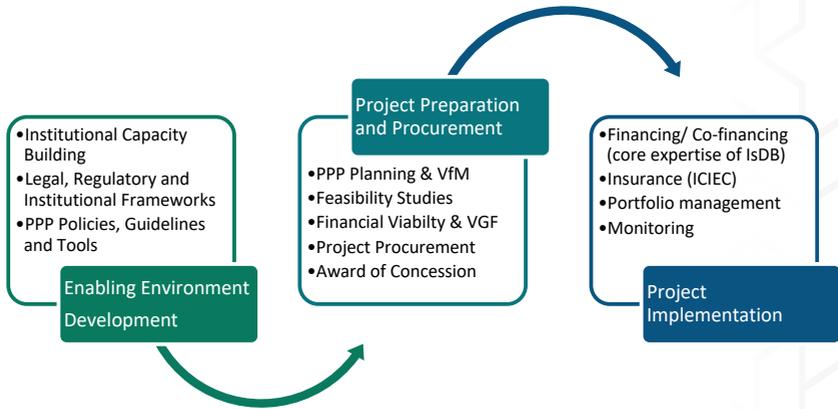
14. The PPP Policy presents the objectives and coverage of IsDB as part of its non-sovereign engagement for PPP and infrastructure finance in MCs. The PPP Strategy will present how to implement the policy objectives and define the organizational approach to implementation.

Figure 2: Manisa 558 bed hospital PPP in Turkey; IsDB arranged 100% Sharia-compliant financing



15. Services to be offered by IsDB will fall across three key areas of support of PPP: enabling environment development, project preparation and project implementation. The following infographic illustrates these areas and relevant interventions within each area.

Figure 3: Scope of services in the PPP space

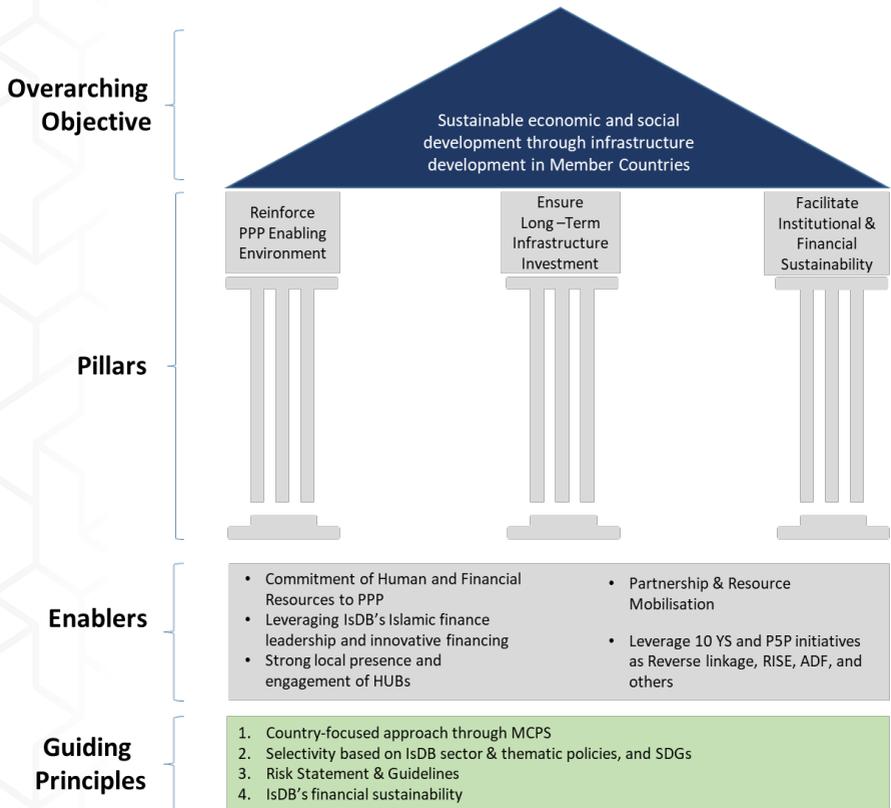


16. IsDB will support MCs across the full spectrum of services as detailed in Figure 3. This support may occur sequentially, beginning with advising on creating or reinforcing the enabling environment, followed by project preparation assistance and financing at a later stage. As well, IsDB may support in any one specific stage.

17. IsDB is positioned to support a MC in any stage of the PPP life cycle, generating momentum to increase opportunities for support in other stages. Helping MCs develop their enabling environment will lead to positive downstream effects in project preparation. Providing upstream advisory would help countries establish a robust pipeline of projects for IsDB to support concessionaires with financing.

18. This model will create significant increase in potential PPP intervention and opportunities for strong partnerships and resource mobilization, leading to greater non-sovereign operations and contribution to the MCs infrastructure development.
19. The implementation of this Policy will be guided by IsDB's thematic and sectoral policies, ensuring full compliance with the institutional requirements as they relate to SDGs, Climate Change, Environmental and Social Safeguards, as well as the Risk Statement and financial sustainability objectives.
20. The **Overarching Objective** is to support MCs to achieve sustainable economic and social development through infrastructure development, which is supported by three key Pillars, five Enablers and four Guiding Principles.

Figure 4: Framework for the PPP Policy



The three identified **Pillars** will support the achievement of the Overarching Objective, as outlined below:

21. Within the first pillar, IsDB will **Reinforce PPP Enabling Environment in MCs**, to establish an ecosystem that is conducive for domestic and foreign private sector investment in infrastructure. An enabling environment would be comprised of laws, regulatory and institutional frameworks and policies which provide a clear basis for PPP projects, as well as fully functioning institutions, vital for mitigating the perceived country and political risks, which are a key constraint.
 - i. Many MCs do not have the enabling PPP legal and regulatory frameworks, suitable institutional framework, or PPP policy. Therefore, the development of a PPP enabling environment, including establishing relevant policies and frameworks, and establishing or empowering relevant government structures and institutions (such as PPP Units), will be a central facet of IsDB advisory support.
 - ii. Support will also include capital market development for mobilization of domestic savings and encouraging institutional investors to channel local currency resources into infrastructure projects through instruments like Project Sukuk, to enhance national participation in PPPs and reinforce long-term sustainability of infrastructure financing.

22. Within the second pillar, IsDB will **Ensure Long-Term Infrastructure Investment** in MCs through partnerships and resource mobilization utilizing all financial products available to IsDB. The use of guarantees and risk insurance products to finance PPP projects is increasing. Guarantees have played an important role in improving the bankability, and facilitating the implementation of PPP projects. As such, the Islamic Corporation for Insurance of Investments and Export Credits (ICIEC) would be expected to play a key role in this respect. IsDB will also seek to create partnerships with international and bilateral institutions and mobilize capital without using its own balance sheet (B loan structure/A B financing).
 - i. Within the MDB community, IsDB is the only provider fully compliant with Islamic financing principles. It is important to note that Islamic financing products suit the philosophy of PPPs as they focus on long term investment, risk sharing, and social development. It has seen a rise in financing infrastructure in large part due to the efforts of the IsDB. IsDB will therefore continue to play a key role in financing PPP projects. Furthermore, it will develop capacity and Sharia compliant instruments to tap into domestic capital markets to raise local currency funding, complementing its foreign currency financing.
 - ii. IsDB has a significant non-sovereign lending portfolio. While PPPs constitute a fair share of this portfolio, other activities cover: (a) Financing public sector companies developing infrastructure; (b) Corporate financing to support large industrial enterprises deemed critical for the economy; and (c) Line of finance to support SMEs. This support is an example of activities

that are creating value to meet IsDB's PPP agenda. Given a strong track record and the contribution to the PPP value chain, non-sovereign infrastructure finance is included within the scope of the PPP Policy.

23. Within the third pillar, IsDB will **Facilitate Institutional Capacity Building & Financial Sustainability for PPP projects** within MCs. This pillar will support enhancing the institutional capacity to identify, assess, plan, implement, award and monitor PPP projects. IsDB will provide advisory support to build institutions founded on principles of transparency and accountability. This area of intervention aims to ensure financial sustainability of infrastructure developed under PPP.

- i. Experience shows that for PPPs to be successfully implemented and thrive in a sustainable manner, counterpart staff in MCs need to have the capacity to identify, develop, procure and manage PPP concessions. As such, IsDB will be proactive in identifying capacity constraints of its MCs and ensuring that capacity building interventions are targeted to address these constraints.
- ii. IsDB will provide support at the project preparation stage to assist MCs to structure bankable PPP projects, by applying established methodologies (VfM analysis, financial analysis/modelling, need for VGF, risk analysis). This allows countries to identify their priorities, encourages private sector participation and sets up a competitive procurement process.
- iii. PPP transaction advisory services would leverage expertise and knowledge to support government clients in assessing, structuring, procuring and closing infrastructure deals. IsDB will also support in developing the oversight capabilities of MCs to ensure proper monitoring and oversight of PPP concessions, which is a critical component of sustainability considering the length of PPP contracts and many stakeholders (public, private, financiers).
- iv. The IsDB would assist in preparing "first in kind" PPP projects, especially in low capacity environments, and in sectors which have a demonstrated track record (such as transport), are easier to implement, and require less expertise by the government. This provides public institutions with experience in PPP which can be applied to more complex projects. With this, IsDB can build capacity and create a model for replication in-country or regionally.
- v. The ability of MCs to structure bankable PPP projects is dependent on the will to introduce market-based user-pay concepts, and the fiscal capacity to provide any public funding or contingent liability support. As part of its support, IsDB will assess the need for VGF and will jointly work with the MC in structuring any VGF funding needs through its sovereign window.

Five Enablers have been identified to support the implementation of the Pillars:

Figure 5: 147 MW Patrind hydropower IPP in Pakistan;
Co-financed by IsDB

24. Commitment of human and financial resources to PPP. There is significant value in supporting MCs in all phases of the PPP project cycle, and providing a range of interventions. However, to do so effectively, substantial financial and human resources need to be allocated to the unit responsible for implementing these activities.



- 25. Leveraging IsDB's Islamic Finance leadership and innovative financing.** IsDB provides Islamic financing which allows for greater risk-sharing. Engagement with MCs will be enhanced to support development of domestic capital markets to route domestic savings into well-structured Islamic products to finance infrastructure. In addition, IsDB will work with domestic and regional Islamic institutions in developing local currency instruments to create co-financing opportunities through structured risk participation strategies.
- 26. Strong local presence and engagement of HUBs.** The needs of MCs are diverse and distinguished. IsDB will offer tailored and targeted support to MCs and leverage its network of Regional Hubs. This regional presence will also allow IsDB to add value by advising MCs in the development of the ecosystem. While the overall direction will be provided from the IsDB headquarters, the regional HUBs must be strengthened with quality human resources in delivery of the mandate.
- 27. Partnership & Resource Mobilization.** Partnership with development partners, MDBs and public institutions within MCs will be targeted. This collaboration will aim to co-finance, mobilize resources, and knowledge sharing through joint institutions, multi-donor trust funds, and facilities. IsDB will play a complementary role in working with partners to jointly finance and support projects. This leadership position in infrastructure finance will be leveraged to create global partnerships to mobilize resources from the Islamic institutions in support of MCs.
- 28. Leverage 10YS and P5P initiatives such as Reverse Linkage, RISE, ADF and project preparation fund.** Several initiatives can support the PPP agenda by offering opportunities to enhance the value addition of interventions. Reverse Linkage can support Pillars 1 and 3 through arrangements for capacity building. Another

example is by pooling national development banks, National Infrastructure Guarantee Funds, and bilateral and multi-lateral development assistance to prepare projects. RISE could play a strong role in providing funding for project preparation. Establishment of facilities to support preparation of PPP projects is a key trend among MDBs, offering financial support for planning and preparing PPP projects, project structuring and marketing, contract preparation, deal negotiation, and post-transaction monitoring and evaluation. In this regard, IsDB will leverage its “PPP Infrastructure Advisory Fund” to assist MCs.

Guiding Principles

The following are four guiding principles governing this Policy:

Figure 6: Queen Alia International Airport, Jordan; Co-financed by IsDB



29. Country-focused approach through MCPS.

IsDB operates in an environment that includes a diverse range of MCs with unique needs and capabilities. Therefore, underpinning all IsDB support to MCs will be MCPS, which will facilitate the development of a tailored PPP support to be offered. Where relevant, linkages with other initiatives of IsDB will be included, such as GVCs. Individual projects would be financed based on the MCPS and the investment strategy associated with the project.

30. **Selectivity based on IsDB’s sector & thematic policies, and SDGs.** Interventions will be guided by sector and thematic policies. The IsDB will formulate support to MCs to meet their commitments under the SDGs in a financially sustainable manner.

31. **Risk Statement & Guidelines.** All IsDB financing, co-financing and project finance comply with the institutional risk statement for non-sovereign interventions. Each financing will be based on sound risk management and risk-return optimization. Beyond the sectors in which IsDB has approved policies, non-sovereign interventions will be guided by the IsDB risk statement and risk guidelines.

32. **IsDB’s financial sustainability.** IsDB’s support will be in line with its financial capacity with a focus on mobilization of resources to leverage its balance sheet through innovative products and partnerships. IsDB’s will leverage its role as an

Islamic finance provider to foster partnerships through specialized products targeting thematically predisposed institutional investors for environment friendly Sukuk, and provide opportunities for MCs to benefit from a larger resource base.

Roles and Responsibilities

33. For the execution of this policy, the goal is to ensure continuity of IsDB's operations by building on its successes and lessons learnt. The PPP Division¹ of the IsDB is the driver of the PPP activities and is at the centre of the PPP agenda. This approach has facilitated the management of PPP activities and created synergies in operations. Non-sovereign infrastructure finance operations are integral parts of this engagement and will continue to be conducted by the Division.
34. There is significant rationale and value for IsDB supporting MCs at all stages of the PPP project cycle. To do so effectively, and to fulfil this mandate, adequate financial and human resources need to be properly allocated to this area of business, both at the Headquarters as well as in select regional HUBs.
35. Close coordination with the other IsDB strategic interventions like RISE, ADF, Resource Mobilization and Reverse Linkages teams, as well as with group entities like ICIEC, will be particularly important to create effective synergies and fully leverage the convening authority of the Bank while maintaining a due process that is delivered in an efficient and transparent manner. The requirement of proper governance and oversight procedures will be introduced within the PPP Strategy to ensure that IsDB adopts best practices and eliminates any duplication of resources or conflict of interest in its own or the operations of its entities.
36. The PPP Policy will be fully aligned with the country programming and the MCPS to ensure that interventions for respective MCs are carefully selected based on needs as well as on available HR resources at the disposal of the PPP Division. Interventions under the PPP Policy will be scaled up over time and prioritization of IsDB's engagement will have to be carefully designed for each MC.

¹ Or any other unit or division in IsDB in case the organizational structure is changed in the future.

Related Policies

37. The PPP Policy is aligned with the 10YS and P5P, and the changing needs of MCs.
38. PPP projects are cross-sectoral, and therefore the PPP Policy is aligned with all sectoral policies within the IsDB: ICT, health, agriculture, education, energy, urban, water, transportation, climate change, and environment and social safeguards. Relevant thematic policies, as well as Procurement and other internal policies will also be adhered to.
39. The IsDB recently developed several strategic initiatives that can play a key role in the PPP agenda of the Bank. Several models for engagement with MCs have been developed to articulate this strategic direction. These include:
- i. **Global Value Chains (GVCs):** Development can be driven by the competitiveness of industries that are connected to the global market through GVCs. This focus on value chains allows the Bank to prioritise its projects in areas with highest impact and at the same time provide greater opportunity for countries to be interconnected through the GVCs.
 - ii. **Regional Infrastructure Supranational Enterprises (RISE):** RISE is an overarching integrated partnership framework aiming to facilitate infrastructure project preparation and implementation. Grounded in the MC's development strategy and IsDB's GVC, the priority infrastructure investments identified in a MC are developed and brought to a bankability stage by RISE.
 - iii. **Alternative Development Finance (ADF):** The Bank's Alternative Development Finance strategies and solutions are aiming to catalyse private investments and non-traditional sector financing for development.
 - iv. **Reverse Linkage:** Defined as a technical cooperation mechanism enabled by the IsDB whereby MCs and Muslim communities in non-MCs exchange their knowledge, expertise, technology and resources to develop their capacities and devise solutions for their autonomous development.

Version History

40. This PPP Policy, is the first PPP Policy developed in the Bank, and is based on the findings of a Technical Paper, which included an analysis of global PPP trends and activities of leading MDBs, a review of IsDB's corporate and sector strategies as well as experience in PPPs and transactions, and an assessment of the key challenges and gaps within MCs that could potentially be met by IsDB services.

41. The PPP Policy will be reviewed periodically to assess implementation experience and to adjust as required considering the evolving needs of MCs and the trends in global markets. Update on the PPP operations of IsDB will be covered under IsDB's annual Development and Effectiveness Report.
42. The PPP Policy shall be effective from the date of its approval by the Board of Executive Directors.

