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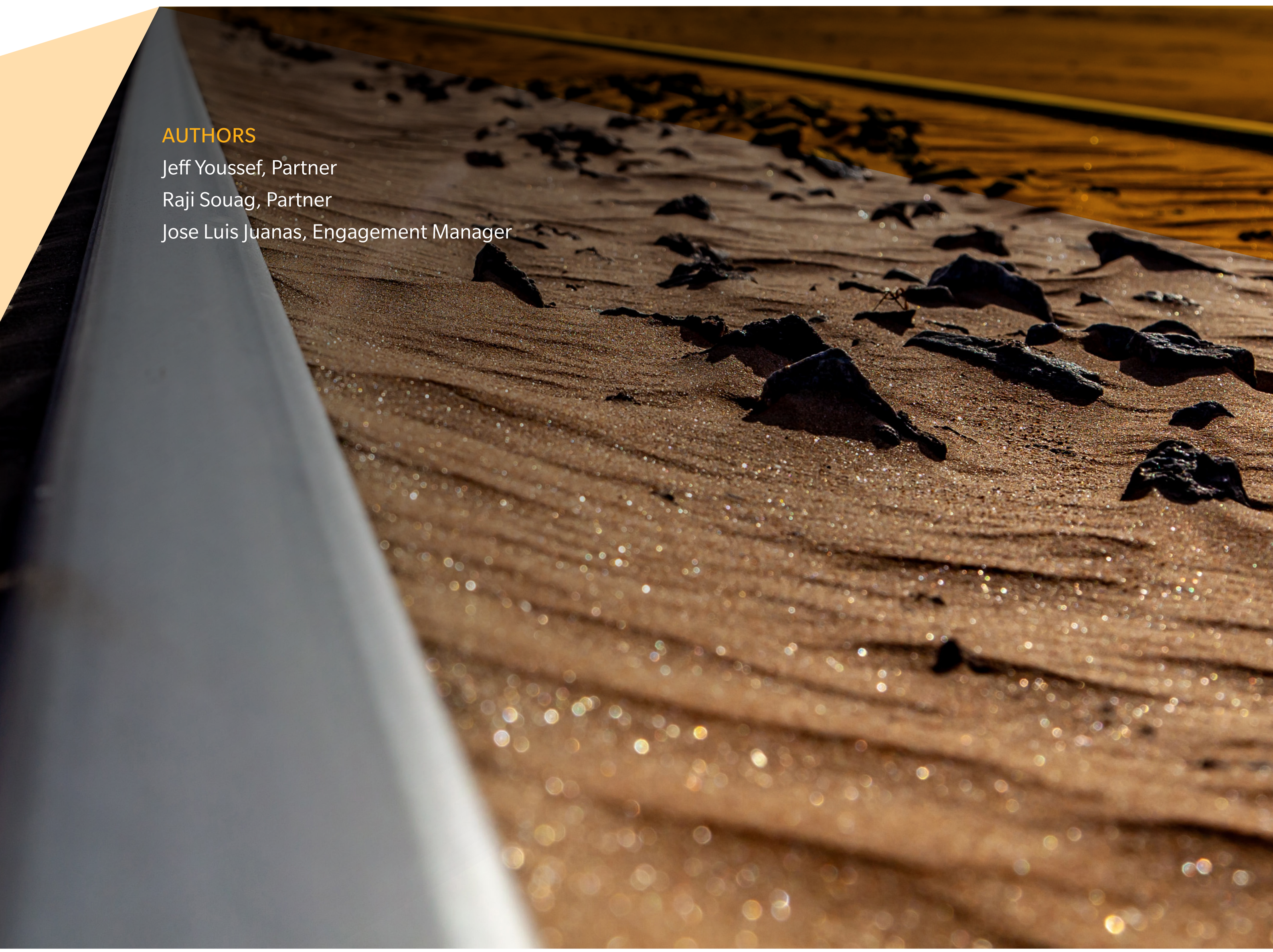
PRIVATE INVESTMENT IS KEY TO UNLOCKING LONG-TERM CAPITAL FOR GULF INFRASTRUCTURE



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EXECUTIVE SUMMARY

A massive gap in how much capital Gulf countries need and what they have available for investment threatens to stifle the region's economic and social development.

The region has prospered economically over the past four decades, and its people have become wealthier. This has resulted in an increasing demand for more – and higher quality – infrastructure.

If the region is to continue along its growth trajectory while simultaneously reducing its reliance on hydrocarbons – as indeed most of the region's national development plans aim to do – more capital must flow into both hard and social infrastructure.

Governments recognize this, but are constrained by funding limitations. A whopping $1 trillion needs to be spent in upgrading and building infrastructure in the next five years in the Gulf, and national governments cannot meet this expenditure by themselves. This means that private investment on a scale hitherto not seen in the region is required to bridge the gap.

That in turn means that national governments must step up efforts to attract investors to a region that still presents tangible impediments to private participation in infrastructure provision and delivery, and one in which the Public Private Partnership (PPP) frameworks are still in their nascency. Compounding matters is the fact that Gulf countries are competing for the same capital with other countries globally that are also looking to upgrade their infrastructures.

The Gulf region has a lot going for it – be it strong economic growth, a young population, the right fiscal conditions, and political stability. Whether it can cash in on this momentum going forward will depend on whether its infrastructure can keep up, and that depends in no small measure on its governments' success in attracting and retaining investment from overseas.

This report examines the trends driving the region's growth and the increased need for more and better infrastructure. It outlines the extent of the funding gap, how the gap can be closed, and the hurdles that need to be cleared in doing so. It places emphasis on the role PPPs can play in helping Gulf countries meet their infrastructure requirements, and the work needed to create a PPP-enabling ecosystem, and more broadly, to foster an investor-friendly environment.

INTRODUCTION: THE GULF'S NEED FOR INFRASTRUCTURE

Three factors are driving the need for infrastructure in the Gulf, including hard infrastructure like transport and utilities, and social infrastructure including health and education systems. These are strong economic growth, rapid population growth, and a young population. If the countries in the region are to live up to their ambitious strategic goals and achieve sustainable growth, they will need to focus on upgrading their infrastructure.

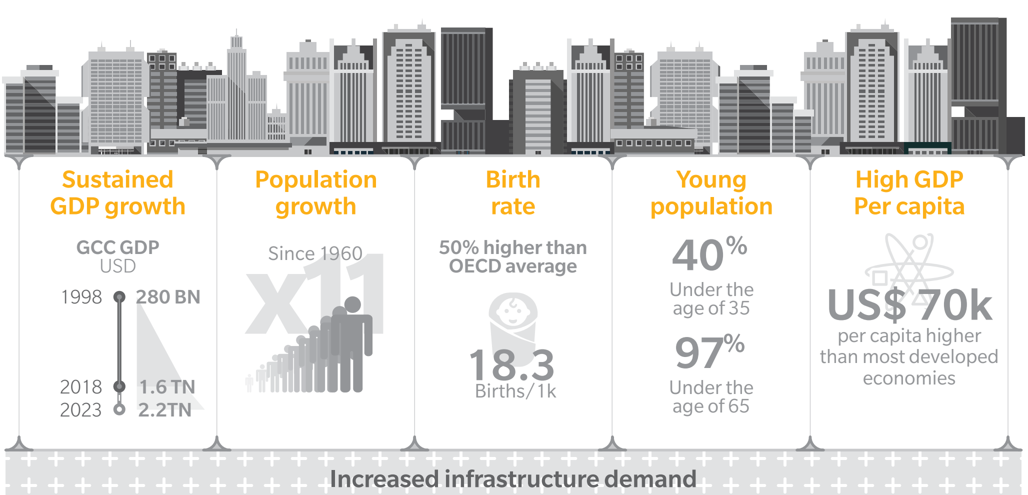
The Gulf region has witnessed strong economic growth for over two decades, with its cumulative GDP increasing from $280 billion in 1998 to $1.6 trillion in 2018. The region is expected to remain a bright spot in the global economy, with its GDP forecast to increase 5.9 percent per annum from 2018 to 2023, according to Oliver Wyman's recent publication *The Arabian Gulf Economies*.

Another defining theme in the Gulf in this period has been the rapid growth in population, which is now 11 times what it was in 1960, and has doubled in the last 20 years to reach 56 million as of 2018. Although the rate of population growth has slowed in the Gulf, it still remains considerably higher than the OECD average.

A third socio-economic strand impacting the demand for infrastructure is the relative youth of the Gulf's population – 4 in 10 people living in the region are under the age of 35, and only 3 percent of the population is over the age of 65.

These three factors, among others, put pressure on existing infrastructure and drive the need for new infrastructure to support these vibrant economies (Exhibit 1). Investment in hard infrastructure – including electricity, ports, and roads – underpins strong economic growth and is essential for it; while investment in social infrastructure – including hospitals and education – is imperative given the young and rapidly growing population in the Gulf.

Exhibit 1: Factors contributing to infrastructure demand in the Gulf



Equally important is the demand for increased infrastructure quality. As the region has benefited from strong economic growth, its population has become wealthier, and that has translated into a demand for better schools, better healthcare facilities, better transportation services, and better access to broadband, for example.

KEEPING PACE WITH GROWTH

Unfortunately, infrastructure development in the Gulf economies has not kept pace with economic advances and the growing population. As a result, most Gulf countries are faced with a substantial infrastructure gap, which cuts across sectors and will have serious implications on the countries' ability to achieve their economic goals.

In transport, for example, significant investment is needed to match the quality and coverage of infrastructure seen in other high-income countries globally. Across the region, it is estimated that Gulf economies will invest around $510 billion in upgrading transportation infrastructure over the next five years, including in ports, airports, railways, and roadways.

A solid transportation network is one of the key pillars of industrial and economic growth and activity, and while governments in Gulf have been improving connectivity, progress has been uneven across the region. Over the past five years, rail, road, and airport infrastructure have attracted around $200 billion in funding, but this is not nearly enough. There are plans afoot to substantially improve existing transport infrastructure and to build new infrastructure to meet ambitious economic development targets. The failure to achieve this can impact companies' supply chains and have implications on international trade, impeding economic growth.

The utilities sector also faces a substantial infrastructure shortfall. In comparison with developed countries, Gulf countries on average fare poorly in terms of utilities infrastructure provision, albeit with significant variations between countries. Take Kuwait for example – it ranks 93rd in the world in terms of electric power and transmission and distribution losses, according to the World Bank. The power sector is instrumental to the continued economic growth of Gulf economies, particularly as they look to diversify away from hydrocarbons, and insufficient power infrastructure will be a bottleneck for economic growth and diversification. Other areas in the utilities sector that deserve increased government attention include water treatment and waste management. In total, it is expected that the Gulf countries will invest about $325 billion in boosting infrastructure development in the utilities sector in the next half decade.

A young and rapidly growing population also puts an increasing amount of stress on the social infrastructure of the region, particularly in the areas of healthcare and building human capital. A growing population means an increasing demand for healthcare and education services. Additionally, as incomes rise rapidly, people want both more and also higher quality hospitals and educational institutions.

Apart from one or two countries, education systems are still developing across the region, impacting the quality of available human capital. Given the increasing impacts of new and emerging technologies on the future of work and the changing nature of work, it is even more important that the youth in the Gulf region are prepared in the best possible way, and provided with the opportunity to acquire skills needed to assume the jobs of tomorrow, as Oliver Wyman's October 2018 study *Maximizing Employment of Nationals in the Gulf* explains.

As importantly, governments must also make sufficient provisions for the reskilling of older workers who may otherwise find it harder to cope with the changing nature of their jobs as technology starts assuming a larger role in both the manufacturing and the services sectors. Between 2019 and 2023, Gulf governments are expected to invest around $70 billion in social infrastructure to meet these requirements.

THE NEED FOR MORE

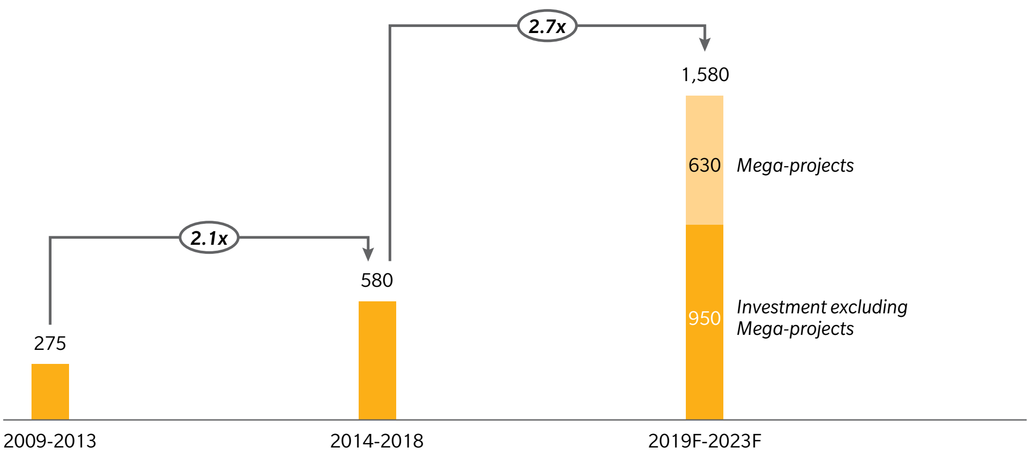
The region's governments are cognizant of this infrastructure challenge, as is evident from several policy pronouncements and their national development plans, almost all of which focus on diversifying their economies away from oil (which will require investments in infrastructure), and the need to build new infrastructure to meet socio-economic development goals.

The strong underlying demand for more infrastructure, and the policy push towards diversification away from hydrocarbons, has resulted in the outlining of very large-scale infrastructure investment plans that are part of the countries' economic transformation plans.

According to our estimates, the cumulative investment required in infrastructure development in the Gulf from 2019-2023 is about $1 trillion, excluding large mega projects such as Neom, Al Hareer City, Qiddiya, Amala, and others. This is 65 percent higher than the total invested in the five years gone by. If mega projects materialize within the currently defined timelines, an additional $600 billion of investment will be required, bringing the total required investment over the five-year period to around $1.6 trillion (Exhibit 2).

Exhibit 2: Infrastructure spending in Gulf expected to grow rapidly

ACTUAL GCC YEARLY INFRASTRUCTURE INVESTMENT[1]
$ BILLION



1. Aggregated 5-year annual spend calculated bottom up aggregating budget of individual projects. Total budget of projects has been uniformly distributed through out the life of the project; Estimates exclude hydrocarbons, telecommunication infrastructure, mining sites, commercial construction, retail, residential, hospitality, & mixed-use construction; 2019-2023 has been forecasted based on the confirmed existing project backlog and historical investment growth.

Source: MEED Projects as at 8th March 2019, Preqin, Oliver Wyman proprietary intelligence on national development plan delivery, Oliver Wyman Analysis

WHERE IS THE MONEY?

There is a need, governments recognize it, and the issue is not whether to invest in more and better-quality infrastructure, but rather how to find the funding to do so.

Governments in the region do not have sufficient funds to meet swelling infrastructure demand, and this puts the focus on their ability to draw private investment to bridge the funding gap. The levels of private investment in infrastructure observed in the Gulf have traditionally been lower than in western jurisdictions.

If the region is to continue growing strongly and fully realize the potential of its human capital, however, this trend cannot continue. As shown earlier, the region needs about $1 trillion in infrastructure investment in the next five years to meet its infrastructure needs, excluding megaproject developments. It is estimated that governments will only be able to fund about $300 billion of the overall requirement from their budgets, leaving a massive funding gap even if state-owned enterprises and sovereign wealth funds step in to prop-up investment in support of governments.

Indeed, private investment to the tune of $400 billion will be needed over the next five years to plug the funding gap if we were to assume that government participation in infrastructure investment will remain at levels seen before (Exhibit 3).

Given this amount is more than what investors are currently likely to be willing to invest in the region, it is possible that some of the planned projects will have to be delayed or postponed owing to funding shortfalls unless significant steps are taken.

But simply opening the door is not enough, as Gulf countries are not alone in seeking to supplement public with private investment. For a while now, the economic fundamentals of the region have remained strong, but there is still intense competition for the private capital that is available in the market, and Gulf countries need to provide a compelling case for this capital to flow to projects and assets in their countries. Many countries in Eastern Europe, South America, and the Asia-Pacific have also made infrastructure development a priority order of business and are striving to draw private capital to meet their infrastructure needs. Some such as Colombia and the Philippines are doing so successfully.

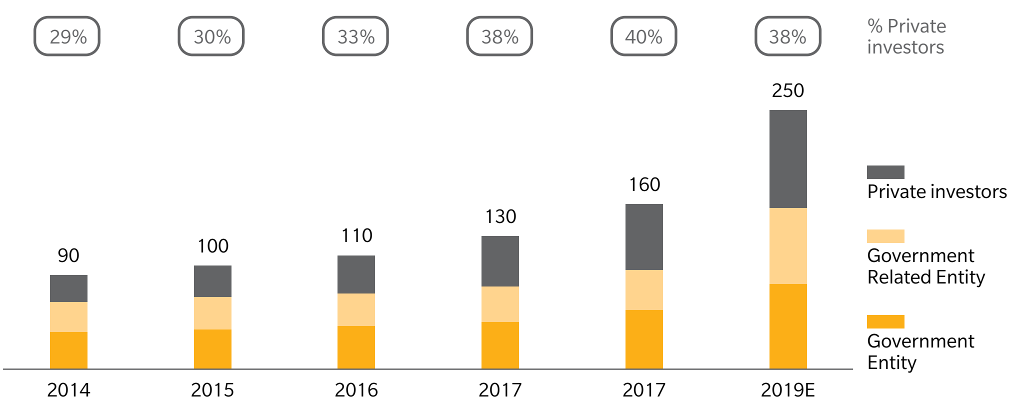
Gulf governments (or indeed governments anywhere) must understand that private capital is not bound by geography or nationalist sentiment. Countries around the world are vying for the same capital as the Gulf countries are, and they are undertaking tricky and difficult reforms to successfully attract private investors.

Indeed, not only is there competition from outside of the Gulf, individual countries within the Gulf must also provide the best possible environment and conditions for private capital. These economies may be bracketed together as part of the Gulf or the Middle East, but private investors are discerning, and will make investment decisions based on various factors, chief among which is government support for private capital.

Only those countries that do a good job of this will be able to raise money from private investors.

Exhibit 3: Who is expected to invest how much?

BREAKDOWN OF INFRASTRUCTURE INVESTMENT BY TYPE OF INVESTOR
$ BILLION



1. Government-related entities include sovereign wealth funds, development funds, and government-owned companies)

2. Private investor participation includes captive funding of infrastructure by corporates (e.g. utility operator funding the development of a power plant, private healthcare providers funding the development of a privately-owned clinic/ hospital etc.). Third party investment is also included as part of the contribution of private investors. However, this is currently marginal relative to contribution of captive private investors.

Source: MEED Projects as at 8 March 2019, Preqin, Oliver Wyman proprietary intelligence on national development plan delivery

CHANNELS FOR PRIVATE CAPITAL

Gulf countries are trying actively to put privatization programs in place, seeking the transfer of ownership, operation, and control of infrastructure assets or facilities from the government to the private sector. Another option is the creation of PPPs, in which the government partners with the private sector and, in most cases, retains ownership of the infrastructure asset (or cedes ownership on a temporary basis). PPPs are, in effect, a means of sourcing private sector capital and expertise for infrastructure development and management.

Without these channels for private investment, projects that are part of the various national development plans may never happen owing to a funding crunch, or they could be faced with severe delays, as seen in many emerging economies around the world where project financing becomes a bottleneck in the building of greenfield infrastructure. Projects could also just simply be cancelled – an undesirable outcome for the governments and people of the region.

PPPs are emerging as the preferred path to bring private investors in to fund major projects, reducing the fiscal burden on governments, and perhaps as importantly, bringing private sector expertise and efficiency to the table. But privatization programs and PPPs require a conducive environment to thrive.

Looking at planned government infrastructure projects until 2040 based on Gulf countries' national development plans (and assuming a 70:30 debt-equity split), forecasts indicate that over the next five years approximately $120 billion of private equity and around $280 billion of private-funded debt will be required. If planned mega projects in the region materialize, then an additional $130 billion in private investment will be necessary.

The region's macroeconomic fundamentals are solid, and it is clear that the underlying demand drivers for infrastructure will continue in the years to come. This is attractive to long-term investors looking for healthy, stable returns. But private participation in Gulf infrastructure has remained at dismal levels historically mainly as a result of an underdeveloped legal and regulatory environment and geopolitical uncertainties.

It is imperative for the region's governments to take steps to bring PPPs into the mainstream. This entails several areas of focus – improve the legal and regulatory framework, enhance the institutional framework, provide financing, and increase government transparency and support for private investors looking to commit to the region. Ultimately, until governments become more investor-friendly, there will be an infrastructure funding deficiency that will result in some landmark projects being put on the backburner or shelved completely, either of which is not ideal.

THERE IS CHANGE

Infrastructure development is one of the key components of the various national development strategies announced by Gulf governments, especially in facilitating the diversification of the region's economies away from oil. To this end, governments have announced major investments in new airports, ports, roads, and rail; more investment in power and utilities, and waste and water management; and in social infrastructure.

The number of PPP projects in the region is also increasing, as governments warm to the idea of greater private investment in the provision and delivery of infrastructure services. Over the past four years (2014-2018) the region has seen substantially more PPP contracts awarded (36), as compared to just 13 from 2011-2014.

Exhibit 4: Private participation in infrastructure is a key component of national development plans

		TOOLS MENTIONED ON THE PLAN		SPECIFIC COMMITTED INVESTMENTS		
Long-term plan	**Short-term plan**	Privatization	PPP	Utilities	Transport	Social infrastructure
Economic Vision 2030 for Bahrain	National Development Strategy 2015-2019	✓	○	○	○	○
New Kuwait 2035	Kuwait Mid-Range Development plan 2015/16-2020/21	✓	✓	✓ Utilities and Water treatment	✓ Rail, ports, airports, roads	✓ Education and Healthcare
Oman 2020 Vision	Five-year Plan 2016-2020	✓	○	✓ Utilities	✓ Rail, ports, airport	○ Goals defined; investments not defined
Qatar National Vision 2030	Second National Development Strategy 2018-2022	✓	✓	✓ Utilities and Water treatment	✓ Rail, ports, airport	✓ Goals defined; investments not defined
Saudi Vision 2030	NTP 2015-2020	✓	✓	✓	✓ Rail, ports, airports, roads	✓ Education and Healthcare
UAE Vision 2021	Strategic Plan 2017-2021	✓	○	✓ Solar PV, Waste-to-energy, Water treatment	○	○

✓ Covered and specific investments are defined as part of the plan

○ Covered but specific investments not defined as part of the plan

Source: National Development Programs of each country, Oliver Wyman Analysis

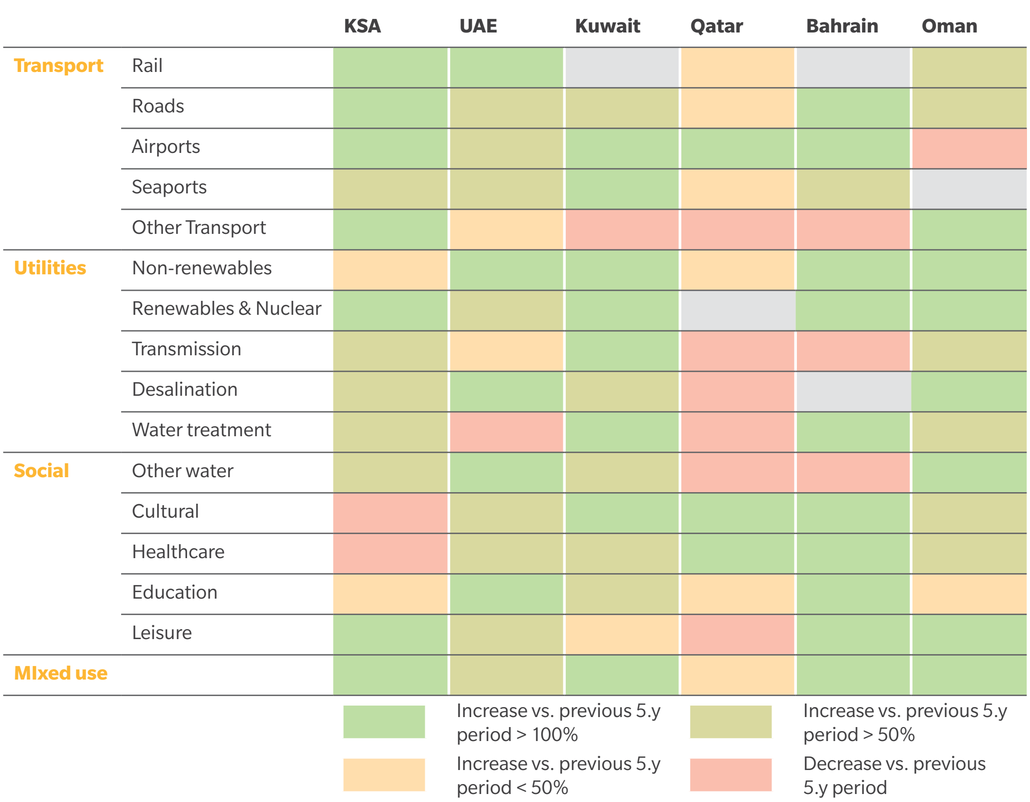
In addition, as of March 2019, 63 PPP projects have either been completed or are under operation in the Gulf countries – this includes projects structured as Build Operate Transfer (BOT), Build Own Operate Transfer (BOOT), Build Own Operate (BOO), Design Build Operate (DBO) or Design Build Operate Transfer (DBOT) with a government body as the procuring authority.

Gulf governments expect both the volume and value of PPP projects to increase over the coming years, with a push across all infrastructure sectors. All national development plans in the region explicitly state that increasing private sector participation is a long-term economic goal (Exhibit 4). They all refer to the privatization of state assets as a tool to achieving this objective.

In their plans, Kuwait and Saudi Arabia explicitly speak about PPPs to enhance infrastructure provision and delivery. That infrastructure is a critical aspect of these national development plans is clear in that the UAE, Saudi Arabia, Kuwait, and Oman have also identified specific projects that will be executed in the coming years in the utilities, transport, renewables, and0social infrastructure sectors.

Exhibit 5: Expected infrastructure investment 2019-2023

% increase over 2014-2018 period



1. Mixed use includes construction of mixed use infrastructure projects (such as NEOM, Red Sea Project, etc.)

Source: MEED Projects as at 8 March 2019, Oliver Wyman Analysis

It is not surprising that all Gulf economies have planned significantly greater investment infrastructure over the next five years as compared to the 2014-2018 period. Exhibit 5 illustrates an over 100 percent increase in spending across several infrastructure subsectors by countries such as Bahrain, Oman, and Kuwait as compared to the previous five years. Saudi Arabia, meanwhile, plans to more than double its investment in railways, roadways, and airports in the next five years, and the Kingdom is expected to see an increase in infrastructure spending across almost all aspects of utilities and transport infrastructure based on the current project pipeline.

Qatar is the only country in the region expected to see a decrease in infrastructure spending across some infrastructure sectors, and this is largely because Qatar has already delivered much of the basic infrastructure linked to the football World Cup, which it is due to host in 2022. As such, infrastructure investment there is expected to remain stable or to decrease across different sectors once its ambitious plans have been realized.

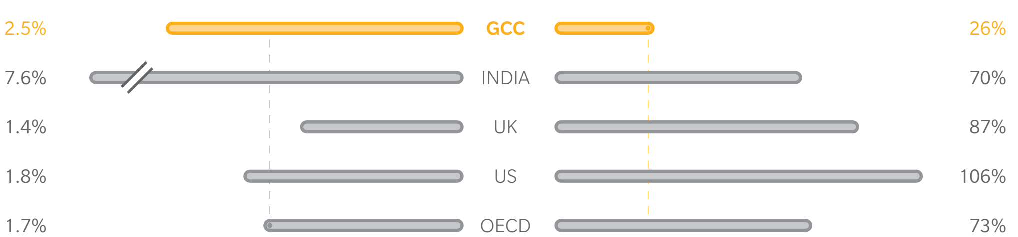
There are also other macroeconomic factors that support the development of PPPs in the Gulf (Exhibit 6):

- Its governments have seen relatively lower debt levels than both developed and emerging economies. The region's debt-to-GDP ratio stood at 26 percent in 2018, compared to 70 percent in India, 87 percent in the UK, 106 percent in the US, or the OECD average of 73 percent;
- The region's economies enjoy very healthy credit ratings too – UAE, Kuwait, and Qatar enjoy credit ratings of Aa2, Aa2, and Aa3 respectively, while Saudi Arabia has a credit rating of A1; and
- Gulf countries' currencies are pegged to the US dollar, resulting in the elimination of forex risk from infrastructure transactions, and generally resulting in higher levels of investor confidence. Importantly, the region's governments have shown a commitment to maintaining their pegs to the US dollar, and this indicates stability in monetary policy.

Exhibit 6: Macroeconomic stability a potential draw for investors (April 2019)

THE GCC IS PROJECTED TO GROW AT ABOVE OECD …
REAL GDP GROWTH RATE, USD, '19 - '23

… AND HAS RELATIVELY LOW DEBT LEVELS …
DEBT-TO-GDP RATIO



… AND INVESTMENT GRADE CREDIT RATINGS AND LONGSTANDING PEGS TO THE USD

	UAE	KUWAIT	QATAR	KSA	OMAN	BAHRAIN
Credit rating	AA2	AA2	AA3	A1	BAA1	B2
Currency pegged to USD since	1978	2003	2001	1986	1986	2001

1. GDP growth forecast as of September 23rd 2019

Source: Moody's, Oxford Economics, World Bank

These three factors provide Gulf countries with a head-start when it comes to attracting investors for PPPs. Low government debt levels indicate high fiscal sustainability, while healthy credit ratings are a sign to investors that their investments are faced with lower levels of financing and sovereign risk, and that governments will not renege on contracts or on their financing responsibilities.

Despite all of this, however, there is still relatively little private sector involvement in infrastructure projects in the region when looked at through the lens of the massive infrastructure gap. Governments must therefore do more to change this.

WHAT MUST GOVERNMENTS DO?

Governments must implement reforms to attract private capital if they don't want to lose out to other regions that are also hungry for investment. They must also help investors understand the risk-return profile of infrastructure investment in their countries. The failure to do so can be ominous for Gulf countries and their people, because the limited private capital available will otherwise find its way elsewhere.

Where should governments start? There are various risks that private investors in PPPs would either want to mitigate completely, or be comfortable assuming. These risks run across the full lifecycle of PPP infrastructure projects, starting from the design and site selection for the project, to construction and operation and maintenance risks, to performance and revenue risks. PPP projects can also be adversely impacted by risks that are not related directly to the projects themselves – these include other market risks, force majeure risks, strategic risks, and political risks. The playing out of one or more of these risks can result in the increase in construction costs, life cycle costs, decreases in revenue and profitability, or even project cancellations.

Governments need to demonstrate they are committed to backing PPP projects and provide private investors who partake in these projects with all the support possible.

Fortunately, the region already has an underlying ecosystem coming into place to facilitate greater PPP investment. Increasingly, global engineering, procurement and construction companies and original equipment manufacturers are participating in the development and operation of infrastructure projects across the Gulf, providing further confidence to private investors who are looking for appropriate partners on the ground.

But all this aside, investors want greater clarity on risk. The first element of this is determining what the risk is, and the second is what premium the investor receives for assuming this risk.

To determine the risk involved in a project (or projects), investors expect the home country to have a clear and binding legal framework for PPPs, an effective mechanism for dispute resolution, and a clear regulatory framework (particularly in the case of monopoly sectors).

Second, for an investor to get a premium for assuming risk, governments must first acknowledge the risk investors are taking on. If they do not do this, private players will either discount what they are willing to pay, or perhaps not invest at all.

The case study below below has a couple of examples of the kinds of risks PPPs are faced with. While each country in the region is unique, the nature of risks that run across them is not. In the recent past, a few projects have run into different kinds of problems, mainly delays and cancellations. While this is not exclusive to the region, the creation of PPP units that catalyze planning across government entities is expected to reduce these challenges going forward.

Exhibit 7: Examples of Infrastructure Projects Experiencing Challenges

REGIONAL EXAMPLE	OVERVIEW OF PROGRAM AND CHALLENGE EXPERIENCED
Landbridge Railway	• Construction of 1,300 rail network including infrastructure works, facilities, signalling systems • Delays in project timelines caused unclear objectives of sponsoring government agencies
KAPP Schools Development Program	• Construction of 9 high-end schools with the objective to improve the quality of educational facilities • Lack of financial analysis led to project cancellation by government sponsoring entity

Again, governments in the region acknowledge this and are strengthening their PPP frameworks, which is a welcome sign. There are efforts afoot to set the necessary regulatory frameworks to attract PPP investment (Exhibit 8). These include provisions to enhance investor protection, including the possibility of international mediation and guarantees around repatriation.

In Saudi Arabia, a Private Sector Participation law is expected before the end of 2019 to distinguish between the Kingdom's privatization and PPP agendas, and to increase investor protection. New processes within this law are also expected to enhance transparency.

Meanwhile, in Kuwait, PPPs have been outlined as a national priority. It has a dedicated unit supporting PPPs and a ministerial committee directly overseeing the PPP agenda. The government is also successfully employing a clear communication strategy that provides ample information on frameworks and upcoming PPP deals.

In the other Gulf countries, while efforts are underway to promote PPP projects, there is either no defined national objectives vis-à-vis PPPs, or an absence of clearly defined strategies and specific targets. A big deterrent in some Gulf countries is the presence of a fragmented legal framework with multiple laws relating to PPPs and the privatization of infrastructure projects. Additionally, there is a lack of investor protection mechanisms and a lack of clarity around risk allocation between different parties. However, government agendas indicate that they are keen to address these issues.

Exhibit 8: Infrastructure policy-related objectives and regulatory developments

	TRANSPARENT AND ALIGNED OBJECTIVES	UNIFIED LEGAL AND REGULATORY FRAMEWORK	EFFECTIVE GOVERNANCE AND MONITORING	CLEAR COMMUNICATION STRATEGY
Bahrain	• Despite recent projects such as the Affordable Housing Project, there are no defined national objectives	• Investor friendly environment (for example, no free zone restrictions, 100% foreign ownership allowed for most activities) • However, no PPP legal and regulatory framework in place • No plans announced to develop specific regulation	• Project level committees established in existing PPP – No centralized governance defined	• Limited publicly available information on PPP framework and upcoming opportunities
KSA	• PPP and privatization sectorial strategies under development • Dedicated 150 FTE agency NCP acts coordinating National Privatization and PPP agenda	• Law 355 and Royal Order 665 govern privatization and PPP • New Private Sector Participation (PSP) law expected by end of 2019 to solve existing gaps (for example, differentiation between privatization and PPP) and increase investor protection (for example, introducing arbitrage)	• Ministries and government agencies are responsible for privatization and PPP • NCP acts as enabler supporting this • New processes to be launched with PSP law will enhance transparency (for example, introduction of project manuals, controlling plan)	• Communication varies depending by agency • NCP increasing transparency to attract international capital
Kuwait	• KAPP's objectives and mandate are clearly outlined – PPP seen as a national priority	• KAPP's legislation includes international arbitrage and simplified processes designed with World Bank	• Dedicated 50 FTE unit (KAPP) supporting PPP • Ministerial Committee directly oversees PPP agenda	• Ample publicly available information on framework and upcoming PPP deals • Az-Zour Phase II tender put on hold without clear reasons
Oman	• PPP considered as national priority, however, no strategy or specific targets defined	• Fragmented legal framework with multiple laws regulating PPP: Privatization law, RD 77/2004, Energy sector law, RD 36/2008 (Tenders Law) • A PPP Law (Decree No. 52/2019) and Privatisation Law (Decree No. 51/2019) recently released in July 2019	• A newly established Public Authority for Privatisation and Partnership (PAPP) has been set up to manage projects	• Limited publicly available information on PPP framework and upcoming opportunities
UAE	• Federal or emirate level strategy not centrally defined • Federal and emirate agencies define their PPP objectives (for example, RTA, ADWA)	• Federal framework defined in UAE Cabinet Resolution of 2017 – law under development • At emirate level legal framework only defined in Dubai (Law 22) • DXB legal framework includes arbitrage	• Coordination by MoF at a federal level • No centralized PPP authority under the Dubai PPP Law – Government entities are required to establish PPP committees for each project	• Varying level of communication transparency depending on government agency/emirate

Source: Government Ministry publications, Oliver Wyman analysis

This is critical for governments if they are to successfully deliver the ambitious infrastructure development programs that they have undertaken. And for this, private capital, discerning as it is, needs to find a compelling reason to commit to the Middle East.

PPPs are long-term contracts that form the basis of long-term relationships between the various stakeholders involved. Building trust and confidence between parties is the foundational pillar for the success of such a relationship. In PPPs, often, it is the private parties who are largely responsible for the design, construction, operation, and maintenance of an infrastructure asset, implying that they are assuming bulk of the development, finance, construction and market risks associated with the project. Governments have the responsibility to make this entire exercise as seamless as possible for investors, and iron out any regulatory and legal issues that can impact the performance of the asset. The key is finding the right balance between the private investors' desire for a satisfactory return and the government's key objective of infrastructure provision for the greater good.

According to World Bank analysis, in terms of PPP regulations and frameworks, Gulf countries are not only still behind developed economies like the US and the UK, but also significantly lagging countries like China and India (Exhibit 9-). This is an issue of concern, particularly in countries such as Qatar and Saudi Arabia, which perform poorly across indicators such as preparation of PPPs, procurement and PPP contract management, resulting in their PPP regulatory frameworks falling well short of what is needed to draw private capital.

That said, change is being seen in both Saudi Arabia and Qatar, as both overhaul their regulatory frameworks. For instance, in addition to a new PPP law expected to come in place this year, Saudi Arabia has also created a dedicated agency to drive its PPP agenda – the National Center for Privatization & PPP, which serves to streamline the private participation process by liaising with other relevant government agencies. Overall, the government's proposed new framework should address some of the pain points for investors and increase confidence in the country. Among other things, Saudi Arabia's new PPP law will contain provisions for investor protection, liberalize investment into healthcare and private education, enable dispute resolution efficiently through arbitration and permit the submission of unsolicited proposals.

While Bahrain and Oman are not covered in the World Bank analysis, there is ample evidence from Oman to suggest that it is on the right track, particularly in the area of PPPs in the areas of energy production and water. In fact, Oman was the first country in the region to establish a PPP in the early 1990s.

But a lot more remains to be done across the region to catch up with developed – and indeed, even developing – economies elsewhere.

Exhibit 9: Comparison of PPP regulatory frameworks[1]

	KSA	UAE[2]	KUWAIT	QATAR	USA	UK	INDIA	CHINA
Preparation of PPPs	34	70	72	31	79	96	82	61
Procurement of PPPs	71	60	71	55	74	86	72	82
PPP contract management	33	52	68	28	57	71	80	76
Unsolicited proposals	*Not Regulated*	42	83	*Not Regulated*	100	*Not Regulated*	*Expressly Prohibited*	54
Ease of doing business ranking (Over 190 countries)	92	11	97	83	8	9	77	46

- Green: PPP score > 70; Ease of doing business ranking < 50
- Orange: PPP score between 50 and 70; Ease of doing business ranking between 50 and 100
- Red: PPP score below 50; Ease of doing business ranking above 100

1. Bahrain's and Oman's framework are currently not assessed.
2. Assessment based on Dubai's PPP legal framework given differences across emirates.
3. Assessment based on Virginia's PPP legal framework given differences across states.

Source: Procuring Infrastructure Public-Private Partnerships - WorldBank, Ease of Doing Business 2019 report – World Bank.

THE ROAD AHEAD

The region is not starting from a clean slate when it comes to private investment in infrastructure – in fact, the first PPP was established in Oman 25 years ago. Between then and now around 90 PPP projects have been awarded. While two in three have been completed or are currently operational, the rest are reported to be under construction. If the past four years are anything to go by, PPPs are becoming a popular vehicle to drive infrastructure development in the region.

While no PPP project in the Gulf has defaulted thus far, there have been projects that have been delayed or cancelled owing to disputes in the tendering process or around investors' repatriation of capital. Given the region's very substantial need for private investment in infrastructure financing, governments must do better to improve the PPP ecosystem in the region. Increasing transparency, streamlining regulatory and bureaucratic processes, and enhancing legal frameworks will go a long way in assuaging investor concerns around investment in the Gulf. Conversely, not doing so successfully will simply mean that private capital will find its way elsewhere at the expense of the Gulf economies.

To maintain momentum and further project their efforts toward sustainable infrastructure funding, Gulf governments should consider the following key steps:

1. **Ensure regulations and PPP laws are in place and are clear:** These laws need to clearly highlight what protection exists for private investors, and what their recourse is in the event of any dispute – contractual or otherwise. Oliver Wyman analysis suggests there is a range of differences in the frameworks across the Gulf countries, but most are looking to improve them.
2. **Ensure that the project pipeline is robust and feasible:** Gulf countries will stand to benefit from a clear process that defines the benefits of a project to investors as well as citizens. Often, a lack of clarity over the intended objectives of a project results in some degree of uncertainty among private stakeholders. The region's countries will profit from an explicit and transparent plan that highlights the rationale of potential PPP infrastructure projects and the value (returns) it can provide to private investors. Governments should avoid project pipelines that can appear like wish lists, which make it difficult for them to be taken seriously.
3. **Ensure acceptable risk-sharing:** PPPs are subject to a variety of risks including design, construction, performance, operations, maintenance, revenue, financial, and political. Governments need to take steps to help minimize the extent of risk a private participant assumes in any PPP project to make a project more palatable to them.
4. **Accept that investors need to make money:** One of the chief challenges associated with any PPP project is creating a win-win scenario for both government and private sector participants. Naturally, given the "public good" nature of infrastructure provision and delivery, governments need to have a "good deal" to provide their citizens. As a result, they are intent on paying less and keeping costs low. But private sector participants need to make money, either for their investors, or shareholders, or both. The sooner governments acknowledge this, the better it will be for the region's infrastructure prospects. Governments must ensure the sustainability of the investor proposition.
5. **Build capabilities to engage with investors:** The push for higher levels of private investment in infrastructure and greater private participation in PPPs has to be accompanied by capability-building within governments to help engage with private investors. The setting up of dedicated PPP units or their equivalents will provide investors with clarity and help them navigate the complicated web of approvals and licenses that may be required from various ministries and government agencies in each country. The governments must play the role of enablers and facilitators by creating an investment-friendly climate and demonstrating long-term commitment.

The Gulf region has the right macroeconomic fundamentals, demographics, fiscal conditions and policy positions in support of greater private participation in infrastructure. To make it count, however, this needs to be backed up with strong government support and commitment to make their economic transformation plans a reality.

Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation.

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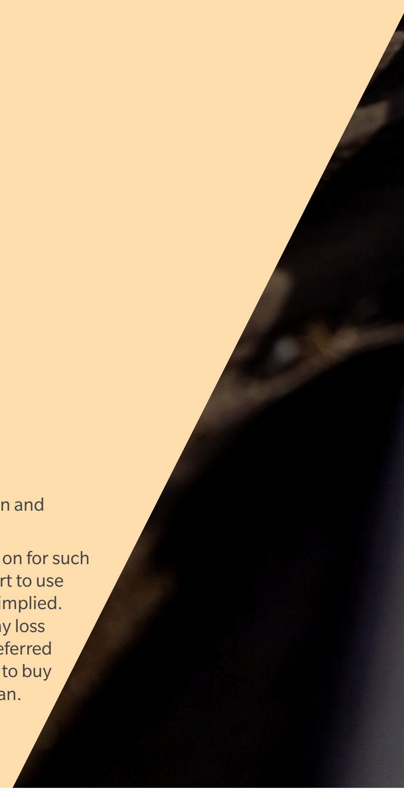

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