ADB

Report and Recommendation of the President to the Board of Directors

Project Number: 49128-002
November 2017

Proposed Loan, Administration of Grant, and Administration of Technical Assistance Grant Islamic Republic of Pakistan: Enhancing Public–Private Partnerships in Punjab Project

Asian Development Bank

CURRENCY EQUIVALENTS
(as of 23 October 2017)

Currency unit	–	Pakistan rupee/s (PRe/PRs)
PRe1.00	=	$0.0095
$1.00	=	PRs105.2500 or £0.7573
£1.00	=	PRs138.9826 or $1.3205

ABBREVIATIONS

ADB	–	Asian Development Bank
ADP	–	Annual Development Programme
ESMS	–	environmental and social management system
GDP	–	gross domestic product
GOPb	–	Government of Punjab
PAM	–	project administration manual
PDD	–	Planning and Development Department
PDF	–	project development facility
PPP	–	public–private partnership
PPPC	–	Public–Private Partnership Cell
RMU	–	Risk Management Unit
TA	–	technical assistance
VFM	–	value-for-money
VGF	–	viability gap fund

NOTE

(i) The fiscal year (FY) of the Government of Pakistan ends on 30 June. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2017 ends on 30 June 2017.

(ii) In this report, “$” refers to United States dollars and “£” refers to pounds sterling.

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CONTENTS

PROJECT AT A GLANCE

1. Basic Data				**Project Number:** 49128-002
Project Name	Enhancing Public-Private Partnerships in Punjab Project	**Department /Division**	CWRD/CWPF	
Country	Pakistan	**Executing Agency**	Planning & Dev. Dept., Govt. of the Punjab	
Borrower	Pakistan			
2. Sector	**Subsector(s)**			**ADB Financing ($ million)**
✓ **Finance**	Infrastructure finance and investment funds			100.00
			Total	**100.00**
3. Strategic Agenda	**Subcomponents**	**Climate Change Information**		
Inclusive economic growth (IEG)	Pillar 2: Access to economic opportunities, including jobs, made more inclusive	Climate Change impact on the Project		Low
4. Drivers of Change	**Components**	**Gender Equity and Mainstreaming**		
Governance and capacity development (GCD) Partnerships (PAR)	Institutional development Public financial governance Bilateral institutions (not client government) Official cofinancing	Effective gender mainstreaming (EGM)		✓
5. Poverty and SDG Targeting		**Location Impact**		
Geographic Targeting	No	Regional		High
Household Targeting	No			
SDG Targeting	Yes			
SDG Goals	SDG8, SDG9			
6. Risk Categorization:	Low			
7. Safeguard Categorization	**Environment:** FI	**Involuntary Resettlement:** FI	**Indigenous Peoples:** FI	
8. Financing				

Modality and Sources	Amount ($ million)
ADB	**100.00**
Sovereign Project (Regular Loan): Ordinary capital resources	100.00
Cofinancing	**19.62**
Government of the United Kingdom - Grant (Full ADB Administration)	19.62
Counterpart	**100.00**
Government	100.00
Total	**219.62**

Note: An attached technical assistance will be financed on a grant basis by the Government of the United Kingdom in the amount of $4,008,724.

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed loan to the Islamic Republic of Pakistan for the Enhancing Public–Private Partnerships in Punjab Project. The report also describes (i) the proposed administration of a grant, and (ii) the proposed administration of technical assistance (TA) for Enhancing Public–Private Partnerships in Punjab, both to be provided by the Government of the United Kingdom for the Enhancing Public–Private Partnerships in Punjab Project, and if the Board approves the proposed loan, I, acting under the authority delegated to me by the Board, approve the administration of the grant and the TA.

2. The Government of Punjab (GOPb), through the Government of Pakistan, has requested the assistance of the Asian Development Bank (ADB) to support public–private partnerships (PPPs) in Punjab by augmenting GOPb's project development facility and the viability gap fund to structure and develop more viable PPP projects that offer value-for-money.

II. THE PROJECT

A. Rationale

3. Economic growth in Pakistan has been hampered by a lack of investment in critical and quality public infrastructure. Public investment on infrastructure has declined over the last decade with the government investing just over 2.1% of gross domestic product (GDP) annually (totaling an estimated $5.7 billion in 2015) towards infrastructure,[1] well below the estimated required annual investment of 7.6% of GDP (equal to $20.6 billion in 2015).[2] This has resulted in inefficiencies across key infrastructure sectors—such as delays in transport of goods and limited access to energy and potable water—which affect both public welfare, and the country's overall industrial and economic growth.

4. Punjab's population of 110 million accounts for about 53% of that of Pakistan; the population density of 536 persons per square kilometer is double that of Pakistan as a whole.[3] Punjab accounts for 60% of national GDP, underscoring its pivotal role for economic growth and employment.[4] Punjab is also undergoing significant urbanization, with a compounded annual urban population growth rate of 3.5% (2007–2015), which is four times the rural population growth rate. The urban population reached 42.9 million in FY2015. Cities are facing challenges due to the significant rural–urban migration, which is increasing demand for public infrastructure. Growing infrastructure investments require broader funding sources from the government, investors and commercial banks, which in the past have shown limited appetite for providing long-dated limited recourse debt to infrastructure projects.

5. To meet these challenges the GOPb increased its Annual Development Programme (ADP) by 15% to an estimated PRs635 billion ($6.0 billion) for FY2018, from PRs550 billion ($5.2 billion) for FY2017.[5] Infrastructure development absorbs 36% of the ADP, and is expected to increase by 13%, to PRs230 billion ($2.2 billion) in FY2018.[6] Social services represent 23% of the ADP, and will increase by 16% to PRs144 billion ($1.4 billion) in FY2018. However, the

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[1] Based on World Bank. Data: Gross Domestic Product estimate for Pakistan of $271 billion for 2015.
[2] The estimated infrastructure investment need is based on the need for the South Asia region, which includes Pakistan. ADB. 2017. *Meeting Asia's Infrastructure Needs*. Manila.
[3] Based on Population Welfare Department, Government of Punjab. Data: Population Profile Punjab.
[4] Punjab Board of Investment and Trade. Punjab at a Glance.
[5] Government of Punjab. 2016. *Development Programme 2016–2017*. Lahore.
[6] Allocation for water supply and sanitation has been included in this estimate.

available budget for public investment in infrastructure is largely insufficient to meet the growing demand. Punjab's infrastructure investment requirement is estimated at about $3.6 billion–$5.0 billion, which significantly exceeds current public capital spending on infrastructure. To address the budget constraints on infrastructure provision, the Punjab government introduced the Punjab Public–Private Partnership for Infrastructure Act (in 2010 and updated in 2014) to augment private sector participation in infrastructure through PPPs.[7]

6. In conjunction with the PPP for Infrastructure Act in 2010, the Punjab government established an institutional framework and guidelines to facilitate the preparation, approval, and implementation of PPPs.[8] A PPP Cell (PPPC) was established within the Planning and Development Department (PDD) to review project proposals (covering technical, operational, and legal compliance to the PPP guidelines), coordinate efforts of line departments, and facilitate the approval of PPP projects by the steering committee.[9] A Risk Management Unit (RMU) within the Finance Department also reviews project proposals, focusing on potential fiscal risks and contingent liabilities emanating from PPP projects. The PPPC serves as the PPP Secretariat for the Punjab government, and submits reviews and recommendations (from the PPPC and the RMU) to the steering committee for approval. Once approved, the line department is responsible for tendering the project, negotiating agreements, and managing project implementation over the term of the concession agreement.

7. The PPPC has a growing project pipeline and about 40 staff members with varying levels of experience and skills that include transaction advisory, projects, policy, communication, and project monitoring. The RMU has one dedicated staff member with some PPP experience, but its capacity to undertake a comprehensive review of financial proposals and concession agreements is insufficient, and capacity building is thus needed. Steering committee members have limited project finance and PPP experience, and are thus likely to rely on the recommendations of the PPPC and RMU. This highlights the need for a more focused subcommittee to review feedback from the PPPC and RMU. The varying levels of skills involved in the Punjab government's PPP framework may result in less-than-optimal structuring of PPPs, and approval of PPPs that offer limited value-for-money (VFM). These projects may potentially expose the Punjab government to unwanted risks over the term of the concession.

8. The Punjab government has a strong pipeline of over 40 projects at various stages of development.[10] Six PPP projects have been awarded since 2010,[11] and two are now operational. Nevertheless, additional resources are required to improve the Punjab government's capacity and deliver more PPP projects that are fiscally sustainable and offer VFM. In some cases, projects receive upfront government support through a viability gap fund (VGF) in addition to operational support in the form of minimum revenue shortfall guarantees.[12] For example, the 70-kilometer Lahore Ring Road Southern Loop Project, a toll road with a 25-year concession costing PRs25 billion ($238 million) awarded in 2016, included (i) upfront VGF support of PRs4.25 billion ($40 million) for land acquisition (for land access not provisioned at no cost by the government under

[7] Punjab Public Private Partnership Act 2014.
[8] Government of Punjab, Planning and Development Department. Guidelines.
[9] Approving authority under the Punjab PPP Act. Composed of 12 members (10 senior government officials from various line departments and 2 private sector members).
[10] List of potential PPP projects that may require VGF support.
[11] Projects include roads, affordable housing, and upgrading of health care facilities. Government of Punjab. Planning and Development Department. Awarded Projects.
[12] The VGF is currently an allocated annual budget item under the GOPb's ADP. The VGF budget is managed by the Planning & Development Department, and monitored by the RMU in the Finance Department. Use of the VGF is approved by the PPP steering committee.

the project),[13] (ii) free provision of land worth PRs4 billion ($38 million) to secure part of the project bank borrowing, and (iii) a guarantee to the concessionaire of 50% of the toll revenue shortfall should actual toll revenue fall below 80% of the estimated toll revenue. Other projects that have not tapped the VGF account for provincial government support have still received public support (provided by line departments in other forms, such as land allocation). Moreover, there is no mechanism for (i) monitoring the contingent liabilities of the government resulting from the PPP projects, and (ii) reflecting these in provincial financial statements.

9. The Punjab government retained a significant portion of project risk under the Lahore Ring Road Project, which may limit its ability to derive VFM in the long term.[14] Ideally, PPP projects should be structured to provide a reasonable balance between the private investor's interests and fiscal prudence. The Lahore Ring Road Project example underscores the lack of appropriate risk-sharing between the private concessionaire and the government, which constrains adequate leverage of scarce public funds. While a few GOPb line departments have developed some experience with PPP projects, large skill gaps exist within line departments that need to be addressed to enhance the flow of benefits to the taxpayers, with transactions rigorously scrutinized through due diligence and a VFM test.

10. To address this issue, the GOPb provides financial assistance to line agencies—through the project development facility (PDF)—to engage transaction advisors.[15] Because capacity of the line departments is limited, the PPPC facilitates discussions with the transaction advisors, aiming to strike a balanced risk-transfer arrangement that limits government contingent liabilities and ensures VFM.

11. The annual VGF budget cannot be rolled over to the following financial year, because there is no dedicated non-lapsable VGF reserved fund account. Also, the GOPb imposes no limits on the value of VGF resources per project, which are at times limited only by the total VGF budget for that financial year. Imposing a limit would ensure greater leverage of VGF resources. The VGF is a powerful tool for leveraging PPPs by (i) providing upfront capital relief to fund project costs to ensure commercial viability, (ii) lowering the cost of capital by providing concessional funding or capital subsidies that do not require future dividends or budget payments, and (iii) supporting operational expenses by providing operational subsidies and/or guaranteeing minimum revenues over the course of the concession.

12. The institutional capacity in Punjab for PPPs needs to be enhanced through (i) improved structuring of eligible PPP projects that offer VFM through a more equitable risk-sharing arrangement, (ii) a sound policy that guides the use of VGF resources, and (iii) strong risk management policies and systems that identify and mitigate potential project and fiscal-related risks emanating from PPP-supported projects.

13. The project is aligned with the ADB Midterm Review of Strategy 2020,[16] in which PPPs are a key driver of change, and the ADB country partnership strategy, 2015–2019 for Pakistan.[17] Lessons from a similar project in Sindh have been considered in the design of this project.[18] Unlike the Sindh project, this project does not propose to establish a separate corporate entity (i.e., a VGF company)—instead, the project will seek to foster governance and accountability in

[13] Land acquisition costs are not capitalized and therefore not recognized as an equity contribution from the GOPb.
[14] The risk transfer arrangement under the project suggests that the GOPb has retained significant funding and operations risks by offering significant upfront support and guarantees during operation.
[15] GOPb allocations for the PDF cannot be carried over to the following fiscal year and lapse if not used.
[16] ADB. 2014. *Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.
[17] ADB. 2015. *Country Partnership Strategy: Pakistan, 2015–2019*. Manila.
[18] ADB. 2016. *Supporting Public Private–Partnership Investments in Sindh Province Project*. Manila.

management of VGF resources. The new VGF guidelines will require that proposals from line departments include a VFM assessment; transaction advisers financed under the PDF will structure PPP deals that offer VFM, and not simply aim to meet investor returns.

14. The decision to adopt an alternative approach to that used in the Sindh project was influenced by the GOPb's reluctance to use a VGF company, because the independence required for risk management and review and monitoring functions is already in place. Separate government departments oversee the PPPC (which is within the PDD) and RMU (within the Finance Department), although some improvements and strengthening of capacity are needed.

B. Impact and Outcome

15. The project is aligned with the following impact: private sector investments and overall employment in Punjab increased.[19] The project will have the following outcome: viable PPP projects that offer VFM increased.[20]

C. Outputs

16. The outputs are (i) PDF and VGF resources for PPP projects augmented, and (ii) PPP institutional capacity enhanced and strengthened.

17. **Output 1: Project Development Facility and Viability Gap Fund resources for public–private partnership projects augmented.** The project will provide financing for the PDF to support line departments in engaging the assistance of experienced transaction advisors. The proposed ADB loan will be used to fund a dedicated VGF window that will be managed by the PDD. VGF guidelines will be established that will specify, among other things, (i) the applicability and use of VGF resource as capital and/or operational support for eligible PPP projects, (ii) a review and approval process (articulating the process flow from application to approval),[21] (iii) VGF restrictions of use (if applicable), (iv) conditions for disbursements of VGF resources to eligible PPP projects, (v) monitoring of performance of VGF-supported projects by the RMU,[22] and (vi) annexes to further articulate key provisions of the VGF guidelines. Furthermore, dedicated non-lapsable accounts for VGF and PDF will be established in PDD, with joint disbursement authorization by Member PPP (PDD board) and Secretary (PDD), to ensure sustainability and continuity of such resources. This will also help streamline the approval process, as it will require an upfront budgetary allocation for GOPb funds, with further budgetary approvals not required after approval by the PPP steering committee.

18. **Output 2: Public–private partnership institutional capacity enhanced and strengthened**. The accompanying TA will support the capacity building component of the project, which will include engagement of procurement and safeguards specialists to strengthen the capacity of the PPPC, and engagement of project finance and contracts management experts to strengthen RMU capacity. These additional resources will improve the government's ability to thoroughly review PPP proposals and draft concession agreements for potential legal risks, contingent liabilities, fiscal risks, and overall VFM, and recommend an appropriate structure and

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[19] GOPb. 2015. *Punjab Growth Strategy 2018: Accelerating Economic Growth and Improving Social Outcomes*. Lahore.
[20] The design and monitoring framework is in Appendix 1.
[21] The use of VGF resources will be reviewed by a steering committee subcommittee, composed of steering committee members who represent the PDD, Finance Department, and private sector. Subcommittee recommendations will be submitted to the steering committee for approval.
[22] Monitoring by the RMU will include review of contingent asset and liabilities, and review and monitoring of covenants, repayments, and/or returns on government support (with respect to the VGF).

approach for PPPs. This enhanced capacity will assist the PPP steering committee's decision-making process when considering PPP proposals. Subsequent to VGF approval, the RMU will monitor the performance of VGF-supported PPP projects and undertake periodic audits and reviews of VGF resources.[23] An environmental and social management system (ESMS) will be established in accordance with ADB's Safeguard Policy Statement (2009), with the PPPC serving as the ESMS focal point for VGF-supported PPP projects. The project will support the engagement of a safeguards specialist for each of several selected line departments,[24] including the ESMS focal point in the PPPC. The VGF may provide support to eligible subprojects, which may include projects that are classified as category A for the environment and resettlement, and that meet ESMS requirements. Institutional capacity at the PPPC, RMU, and selected line departments will be strengthened through the accompanying TA. The TA will also support information sessions on PPPs to help identify and address impediments to private sector participation, thereby promoting the sharing of knowledge regarding, and the sustainability of, PPPs in Punjab.

D. Summary Cost Estimates and Financing Plan

19. The project is estimated to cost $219.6 million (Table 1).

20. Detailed cost estimates by expenditure category and by financier are included in the project administration manual (PAM).[25] The majority of the project cost (up to $200.0 million) provides funding for the VGF to support and improve the commercial viability of eligible PPP projects, with support also provided ($8.4 million) to fund the PDF to assist selected line departments engage external transaction advisors to help prepare PPP projects.

Table 1: Summary Cost Estimates
($ million)

Item			Amount[a]
A. Base Cost[b]			
	1.	Project Development Facility	8.4
	2.	Viability Gap Fund	200.0
		Subtotal (A)	**208.5**
B. Contingencies[c]			**2.9**
C. Financing charges during implementation[d]			**8.2**
		Total (A+B)	**219.6**

[a] Exclusive of taxes and duties imposed in the territory of the borrower.
[b] In mid-2017 prices.
[c] Price contingencies computed at average of 15% to include provision for potential exchange rate fluctuation.
[d] Includes interest and commitment charges. Interest during implementation for the ordinary capital resources loan has been computed at the 5-year US dollar fixed swap rate plus an effective contractual spread of 0.50%. Commitment charges for the ordinary capital resources loan are 0.15% per year to be charged on the undisbursed loan amount.
Note: Numbers may not sum precisely because of rounding.
Source: Asian Development Bank estimates.

21. The government has requested a regular loan of $100 million from ADB's ordinary capital resources to help finance the project. The loan will have a 20-year term, including a grace period of 5 years; an annual interest rate determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility; a commitment charge of 0.15% per year; and such other terms and conditions as set forth in the draft loan and project agreements. Based on the straight-

[23] With the assistance of external auditing firms.
[24] The selected line department will include: (i) the Health Department, (ii) the Communications and Works Department, and (iii) the Housing Urban Development and Public Health Engineering Department.
[25] Project Administration Manual (accessible from the list of linked documents in Appendix 2).

line method, the average maturity is 12.75 years, and there is no maturity premium payable to ADB.

22. The summary financing plan is in Table 2. ADB will finance the expenditures in relation to the VGF funding. The Government of the United Kingdom, through the Department for International Department, will provide grant cofinancing equivalent to $19.6 million, to be administered by ADB.

Table 2: Summary Financing Plan

Source	Amount ($ million)	Share of Total (%)
Asian Development Bank		
Ordinary capital resources (regular loan)	100.0	45.5
Government of the United Kingdom (grant) [a]	19.6	8.9
Government of Pakistan	100.0	45.5
Total	**219.6**	**100.0**

[a] Cofinancing is administered by the Asian Development Bank. This amount includes bank charges and a provision for foreign exchange fluctuations (if any), to the extent that these are not covered by the interest and investment income earned on this grant. The grant amount excludes administration fees and other charges as may be deducted pursuant to the cofinancing agreement. Estimated using the exchange rate of £1 = $1.2845 on 14 July 2017.
Note: Numbers may not sum precisely because of rounding.
Source: Asian Development Bank estimates.

E. Implementation Arrangements

23. The PDD will be the executing and implementing agency for the project. The PPPC will be the implementing unit and will be supported by the RMU. The PDD will manage and administer the VGF resources, and the RMU will monitor the performance of VGF-supported PPP projects in accordance with the VGF guidelines. The PDF resources will be administered by the PPPC in accordance with the PDF guidelines to support selected line departments to engage experienced external consultants and transactions advisors to prepare and execute PPP projects.[26] The PPPC has been administering PDF support to various line departments since 2010. Institutional capacity at the PPPC, RMU, and selected line departments will be strengthened through the accompanying TA (para. 26).

24. The executing and implementing agency will not be directly involved in implementing the physical delivery of approved PPP projects. The relevant line departments will procure the PPP projects, and will legally enter into the respective concession agreements with the selected private sector concessionaires. Procurement undertakings related to the ADB loan, including the ADB-administered grant and TA grant, will follow procedures pursuant to ADB's Procurement Guidelines (2015, as amended from time to time) and ADB's prior review (as required). Because the project will be cofinanced by the Government of the United Kingdom and administered by ADB, universal procurement will be applied.[27]

25. The implementation arrangements are summarized in Table 3 and described in detail in Diagram 1 of the PAM (footnote 25).

[26] Government of Punjab. Planning and Development Department. *Guidelines for the Project Development Facility for Public–Private Partnerships in Infrastructure*.
[27] ADB. 2015. *Enhancing Operational Efficiency of the Asian Development Bank*. Manila.

Table 3: Implementation Arrangements

Aspects	Arrangements
Implementation period	January 2018–December 2022
Estimated completion date	31 December 2022
Estimated loan closing date	30 June 2023
Management	
(i) Executing agency	Planning and Development Department, Punjab
(ii) Key implementing agency	Planning and Development Department, Punjab
(iii) Implementation unit	Lahore, PPP Cell (with assistance and support from the Risk Management Unit)
Disbursement	The loan proceeds will be disbursed following ADB's *Loan Disbursement Handbook* (2017, as amended from time to time) and detailed arrangements agreed between the government and ADB.

ADB = Asian Development Bank, PPP = public–private partnership.
Source: Asian Development Bank.

III. ATTACHED TECHNICAL ASSISTANCE

26. The loan will be accompanied by a transaction (TA) for Enhancing Public–Private Partnerships in Punjab to address skill and resource gaps in the relevant government agencies. The PDD will be the executing agency for the TA. The TA will assist in reviewing PPP project proposals requiring VGF support, providing recommendations to the steering committee, and monitoring the performance of those projects. The TA will also help facilitate the evaluation of PPP project proposals by selected line departments, and monitor projects in accordance with the ESMS and other relevant regulations. The TA outputs are (i) improved capacity of the PPPC and RMU, (ii) improved capacity of selected line departments, and (iii) enhanced accountability and governance of the VGF.[28] The TA will commence immediately after approval to meet provisions under loan effectiveness.

27. The TA is estimated to cost $4,450,000, of which $4,008,724 (£3,120,844 equivalent)[29] will be financed on a grant basis by the Government of the United Kingdom and will be administered by ADB. The TA consultants will be engaged by ADB in accordance with ADB's Guidelines on the Use of Consultants (2013, as amended from time to time). TA funds will be disbursed in accordance with ADB's *Technical Assistance Disbursement Handbook* (2010, as amended from time to time). The indicative implementation time frame for the TA will be from November 2017 to December 2022.

IV. DUE DILIGENCE

A. Economic and Financial

28. Infrastructure investment for Punjab must be financed in part by non-public capital spending, including funding from the private sector, which has been investing in energy, telecom, and other sectors. Procurement of public infrastructure and services through PPPs offers opportunities to bridge Punjab's infrastructure gap.

29. The $100 million in ADB support to augment Punjab's VGF resources has the potential to raise $200 million to $300 million in additional PPP funding for infrastructure development over

[28] Attached Technical Assistance (accessible from the list of linked documents in Appendix 2).
[29] Exchange rate as of 14 July 2017.

the project implementation period.[30] Private sector infrastructure financing can bridge the financing gap and help alleviate poverty through the jobs created by such investments. It can also ease fiscal constraints faced by the government by allowing the private sector to assume part of the financing burden for public infrastructure development. The introduction of private sector expertise through PPPs may also hasten the completion and enhance the efficiency of infrastructure project operations.

B. Governance

30. The financial management risk rating, before risk mitigation measures, is considered *substantial*; it is assessed as *moderate* taking into account the risk mitigation measures. The public expenditure and financial accountability assessment of 2012 rates the budget credibility of the province as *low*. The controller general of accounts has major responsibilities for accounting, pre-audits, and payments. The GOPb is working to form a provincial internal audit authority, but the only internal audit mechanism currently available is the pre-audit of transactions by the office of the provincial accountant general. The integrated fiscal monitoring system with consolidated direct and contingent liabilities relating to PPP projects is weak. The governance, risk management, and operational policies and procedures in the existing PPP framework for VGF are inadequate, due to the absence of VGF guidelines in the framework. The oversight of the PDF and VGF need to be improved. Actions required under the project include: (i) establishment of non-lapsable reserve fund accounts for PDF and VGF, in which government funds are transferred as block releases; (ii) confirmation that accounting and reporting systems for the PDF and VGF are satisfactory to ADB in terms of transparent and reliable financial reporting; (iii) periodic external audits of VGF and PDF utilization carried out by a firm of chartered accountants acceptable to the GOPb and ADB; and (iv) establishment by the RMU of a system to monitor direct and contingent liabilities related to PPP contracts.

31. The PDD, as the executing and implementing agency, will use the ADB Procurement Guidelines for all institutional procurement, and ensure that procedures acceptable to ADB are followed when (i) private entities are selected through competitive bidding procedures; (ii) private entities apply their own procedures for procurement of goods, works, and consulting services; and (iii) line departments engage consulting services financed from the PDF acceptable to ADB. ADB will provide support for engagement of procurement expert(s) under the accompanying TA to assist the PDD with procurement activities. The resulting procurement risk is low, as private entities will follow procurement procedures acceptable to ADB. The ADB Anticorruption Policy (1998, as amended to date) was explained to and discussed with the government and the PDD. Policy requirements and supplementary measures are specified in the PAM (footnote 25).

C. Poverty, Social, and Gender

32. Punjab has a 31% poverty rate; deteriorating infrastructure and social services brought about by funding constraints; and wide economic, social, and political gender disparities. PPPs are an alternative means of procuring public infrastructure through private sector participation and will help address these problems. The project is categorized as effective gender mainstreaming, and is expected to produce PPP projects with significant social benefits, especially for vulnerable groups, such as the poor, women and girls, children, the elderly, and people with disabilities. Social impact assessments that include gender as a key parameter will be required for PPP project proposals. Gender training for PPPC and RMU staff will assist in assessing PPP proposals with regard to social and gender issues. Screening guidelines and tools will incorporate social and gender criteria, and women will participate in PPP training.

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[30] On the basis that average gearing offered by commercial banks for a PPP project may be 60% to 70%.

D. Safeguards

33. In compliance with the ADB Safeguard Policy Statement, the project is categorized as financial intermediary for the environment, involuntary resettlement, and indigenous peoples.[31] The projects requiring VGF support may include projects that are category A for the environment and resettlement but C for indigenous peoples (no indigenous or tribal peoples live in or around the project areas). The PDD will need to establish and maintain an ESMS acceptable to ADB that fully incorporates the safeguard requirements (SR 1–3, including information disclosure and consultation) of ADB's Safeguard Policy Statement.[32] Subprojects will not be eligible for ADB financing if they appear on ADB's Prohibited Investment Activities List. The PDD will ensure the ESMS is in place prior to ADB's first disbursement for the financing of eligible projects.

34. PDD staff resources and skills will be strengthened by engaging environmental and resettlement specialists at the PPPC and selected line departments under the TA. Safeguards specialists hired under the TA will provide PPP training in ESMS implementation and monitoring, and will assist and enable the PPPC and selected line departments to manage the ESMS, and comply with operational guidelines on environment and social policies, safeguards screening, categorization and review procedures, and oversight during subproject implementation. The ESMS will be periodically audited and reviewed by external, independent, certified auditors; reports (including environmental impact assessments, land acquisition resettlement plans, and environmental management reports) will be disclosed in line with ESMS and ADB Safeguard Policy Statement disclosure requirements.

E. Summary of Risk Assessment and Risk Management Plan

35. Overall project risks are assessed as medium. Significant risks and mitigating measures are summarized in Table 4 and described in detail in the risk assessment and risk management plan.[33]

Table 4: Summary of Risks and Mitigating Measures

Risks	Mitigating Measures
Deteriorating local security reduces private sector confidence and interest in PPP projects	The government is making a strong effort to address local security issues. This is outside the scope of the project, and appears not to have influenced investment decisions by some local and international investors.
Political influence results in approval of PPP projects that may not offer VFM	A steering committee decision to proceed with a project deemed and classified as not offering VFM and not complying with ESMS requirements will disqualify that project from receiving ADB-funded VGF support.

ESMS = environmental and social management system, PPP = public–private partnership, VFM = value-for-money, VGF = viability gap fund.
Source: Asian Development Bank

V. ASSURANCES AND CONDITIONS

36. The government and GOPb have assured ADB that implementation of the project shall conform to all applicable ADB policies, including those concerning anticorruption measures, safeguards, gender, procurement, consulting services, and disbursement as described in detail in the PAM and loan documents.

37. The government and GOPb have agreed with ADB on certain covenants for the project, which are set forth in the loan agreement and project agreement.

[31] ADB. Safeguard Categories. https://www.adb.org/site/safeguards/safeguard-categories.
[32] ADB. 2009. Safeguard Policy Statement. *Operations Manual.* OM F1. Manila.
[33] Risk Assessment and Risk Management Plan (accessible from the list of linked documents in Appendix 2).

38. The standard conditions for loan effectiveness will be supplemented by additional conditions for withdrawals from the loan account, which include (i) VGF guidelines (in form and substance acceptable to ADB and GOPb) are formally adopted and notified by GOPb and incorporated into the standard operating procedures of the RMU; (ii) the RMU is adequately staffed for VGF monitoring; (iii) GOPb has established the ESMS and has adequate staff for implementation and monitoring of the ESMS for PPP projects; and (iv) dedicated VGF and PDF accounts are established in a manner acceptable to ADB (ringfenced from other GOPb accounts used for infrastructure-related expenditures).

VI. RECOMMENDATION

39. I am satisfied that the proposed loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan of $100,000,000 to the Islamic Republic of Pakistan for the Enhancing Public–Private Partnerships in Punjab Project, from ADB's ordinary capital resources, in regular terms, with interest to be determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility; for a term of 20 years, including a grace period of 5 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft loan and project agreements presented to the Board.

Takehiko Nakao
President

23 November 2017

DESIGN AND MONITORING FRAMEWORK

Impact the Project is Aligned with Private sector investments and overall employment in Punjab increased (Punjab Growth Strategy, 2018)[a]			
Results Chain	**Performance Indicators with Targets and Baselines**	**Data Sources and Reporting Mechanisms**	**Risks**
Outcome Viable PPP projects that offer value for money increased	a. By 2023: Private investment through PPPs for the provision of provincial infrastructure and service projects increased to 10% of the annual development program (2015–2016 Baseline: percentage of PPP projects in annual development program 6.3%)	a. Finance Department reports; PPPC status reports; PPP projects awarded as disclosed in PPPC website	Unexpected deterioration of security situation
Outputs 1. PDF and VGF resources for PPP projects augmented	1a. Twelve PPP project proposals with PDF support submitted and reviewed by the RMU and the PPPC by 2022, with at least one social project approved with direct benefits to vulnerable groups such as the poor, women, girls, elderly, and persons with disabilities (2017 baseline: 0) 1b. Five PPP projects awarded with VGF support by 2022 (2017 baseline: 1)	1a.–b. PPPC reports; ADB review mission reports; updates as disclosed in PPPC website	Unfavorable political influence over the approval of PPP projects that may not offer VFM
2. PPP institutional capacity enhanced and strengthened	2a. VGF guidelines approved by steering committee and adopted and made operational by March 2018 (2016 baseline: Not applicable) 2b. ESMS, with social and gender indicators, established and adopted by March 2018 and prior to first disbursement. (2016 baseline: No ESMS) 2c. At least three PPP training programs delivered to relevant government agencies, with women accounting for 20% of participants from at least one department, by 2022. (2017 baseline: No PPP training arrangements in place) 2d. At least three locally held PPP investment conferences delivered to increase awareness from prospective private investors by 2022 (2017 baseline: No local conference held in Punjab)	2a. PPPC reports; relevant Government of Punjab notification; ADB review mission reports 2b. PPPC reports; ADB review mission reports 2c. Training calendar and reports 2d. Investment conference reports and coverage	

Key Activities with Milestones
1. PDF and VGF resources for PPP projects augmented 1.1 Draft and approve VGF guidelines by March 2018. 1.2 PPPC to identify at least three PPP projects in the pipeline that require PDF and VGF support by March 2018. **2. PPP institutional capacity enhanced and strengthened** 2.1 Administer and manage VGF resources in accordance with VGF guidelines (ongoing from March 2018 until 2022). 2.2 Establish ESMS with PPPC as focal point by March 2018. 2.3 PPPC to provide capacity support (as required) to selected line departments in project identification and proposal development (ongoing and as required until 2022). 2.4 Develop and implement PPP training plan for relevant government agencies by March 2018. 2.5 Develop and implement plan for investment conference events by June 2018. 2.6 Engage experts (including project finance and contract management specialists in the RMU, and procurement and safeguards experts in the PPPC) by March 2018. 2.7 In conjunction with 2.6, engage additional resources for safeguards implementation and compliance (social and environmental experts) at selected line departments by March 2018.
Inputs
ADB: $100 million (regular ordinary capital resources loan) Government of Pakistan: $100 million (equivalent) Government of the United Kingdom (grant): $19,616,025 (equivalent); and (technical assistance) $4,008,724 (equivalent)
Assumptions for Partner Financing
Not applicable

ADB = Asian Development Bank, ESMS = environmental and social management system, PDF = project development facility, PPP = public–private partnership, PPPC = Public–Private Partnership Cell, RMU = Risk Management Unit, VFM = value-for-money, VGF = viability gap fund.

[a] Government of Punjab. 2015. *Punjab Growth Strategy 2018: Accelerating Economic Growth and Improving Social Outcomes*. Lahore.

Source: Asian Development Bank.

LIST OF LINKED DOCUMENTS
http://www.adb.org/Documents/RRPs/?id=49128-002-3

1. Loan Agreement
2. Project Agreement
3. Grant Agreement: Externally Financed
4. Sector Assessment (Summary): Finance
5. Project Administration Manual
6. Contribution to the ADB Results Framework
7. Development Coordination
8. Attached Technical Assistance Report
9. Economic and Financial Analysis
10. Country Economic Indicators
11. Summary Poverty Reduction and Social Strategy
12. Gender Action Plan
13. Financial Intermediary: Environmental and Social Management System Arrangement
14. Risk Assessment and Risk Management Plan