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Kuwait's PPP Law

Research Highlights:

A robust PPP legal framework can help increase private firm participation and bridge funding gaps in a country. This report analyses whether the Kuwait PPP law can help accomplish such objectives.

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POLICY & REGULATORY RESEARCH REPORT

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Overview, Amendments and Status of the PPP Law

The PPP (Public Private Partnership) model has gained traction in recent years. The PPP model enable governments to efficiently execute large-scale, complex projects that are capital intensive. With PPP model, governments are able to tap into financial resources and expertise of private players by sharing risks, resources, responsibilities and rewards.

The year 2014 witnessed a big push in reforms momentum as the Kuwaiti government introduced new PPP laws repealing the old ones. The new laws are primarily designed to redress the issues and challenges faced under the virtue of previous laws and regulatory scene. The new PPP laws are mostly seen as a further strategic impetus to the ongoing economic diversification drive begun against the backdrop of sliding oil prices and massive share of oil revenues in the economy.

It's been observed that PPP laws in Kuwait are one of the most investor friendly and attempting to create fair and level playing field for the businesses to operate and private sector to augment further. However, this is yet to reflect in terms of projects gained under PPP format. Major hurdles cited includes financing constraints, complexities in the bidding process, procurement problems and lack of clarity over projects pipeline. This has resulted in delays in a number of important projects in the country.

In this research note we have tried to evaluate project financing options that can be used to effectively execute these PPP projects. We have also briefly looked at the regulatory frameworks being used by other countries in the region to execute PPP projects.

Currently, UAE and Kuwait have successfully announced full-fledged PPP laws and have projects functioning on those legal frameworks. Saudi Arabia, Bahrain and Oman are still in the process of announcing complete legal framework for the PPP sector although Saudi Arabia in 2018 announced draft laws for consultation indicating possible implementation of the laws shortly.

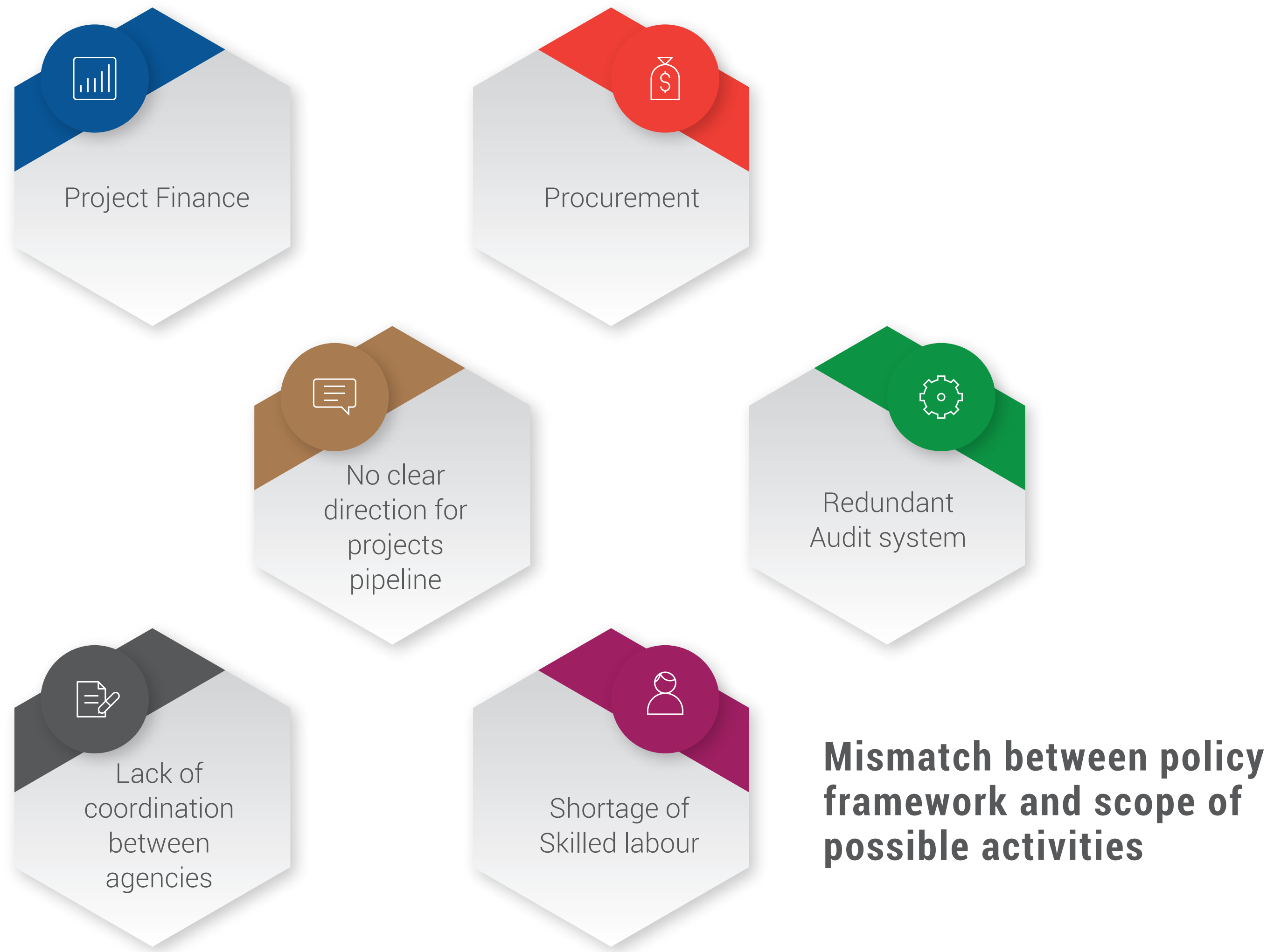
The PPP wave has encapsulated the public assets procurement mechanism in most of the GCC countries where PPP has been viewed as a potential solution to procurement woes because currently fiscal budgets across the GCC countries are financially congested mainly due to oil price volatility.. An uneasy economic environment prevails across the GCC oil exporter countries, which must adjust to the new reality of volatile oil prices. Policy-makers are implementing tough decisions, austerity measures like reductions in public spending and the introduction of taxes and economic reforms (privatization, trade liberalization, removal of barriers to competition and so on) that will certainly impact the region[1].

Hence policy action is more active in PPP area in order to leverage the domain and thereby thrust growth in the private sector.

The project landscape of GCC is constrained at the moment with many project cancellations. Total value of contract being awarded dropped by 8% in 2017 compared to 2016 when drop rate in value of contracts awarded was low by 32% compared to 2015. In 2017 Kuwait cancelled the second phase of Al-Zour North Independent water and project[2]. Furthermore during the same year, the Saudi Arabian authorities cancelled project worth US$ 13.3 bn[3].

[1] Construction Weekly 2018
[2] MEED 2017
[3] Gulf Business 2017

Major bottlenecks in PPP Environment in Kuwait



Source: Marmore Research

1 Understanding Public Private Partnership (PPP)

1.1 Introduction

Most developing countries across the globe face the challenges in the form of meeting the growing demand for new and better infrastructure services. The public sector has restricted resources for funding from the customary sources and has capacity constraints to implement a number of projects in parallel. Therefore, to upgrade the existing infrastructure facilities and implement new services, governments have realized that partnership with the private sector is a viable option.

In a PPP program, the partners, based on some form of a legal contract, decides to assign tasks associated with the infrastructure project's execution and/or operation and management. This collaboration or partnership is built on the expertise of each partner that meets clearly defined public needs through the appropriate allocation of:

- Resources
- Risks
- Responsibilities, and
- Rewards

1.2 Advantages of PPP Projects

The logic for public sector's increasing alliance with the private sector for implementing and involving in such infrastructure services is primarily because of:

- Increased efficiency in project delivery, and operation and management;
- Availability of additional resources to meet the growing needs of investment in the sector; and
- Access to advanced technology (both hardware and software).

Properly executed planning and development of a project also allows better screening of options, and helps in deciding appropriate project structure and choice of technology considering cost over the whole life cycle of the project.

1.3 PPP project types

We have witnessed increasing trends towards the public sector calling private sectors to provide basic and complex infrastructure services that were once delivered by the public sector in:

- Large infrastructure projects
  a. Energy and power
  b. Communication
  c. Transport
  d. Water sectors
- Real-Estate development projects
  a. Residential units
  b. Educational institutes
  c. Tourist places

1.4 Types of private sector participation in public projects

A wide array of PPP models have surfaced. These models vary mainly by:

- Ownership of capital assets;
- Responsibility for investment;
- Assumption of risks; and
- Duration of contract.

There are various models of PPP being used. However, there are mainly five general categories exist based on the increased involvement of and risks for the private sector. The five broad categories are[4]:

- Supply and management contracts
- Turnkey contracts
- Leases
- Concessions
- Private Finance Initiative (PFI) and Private ownership.

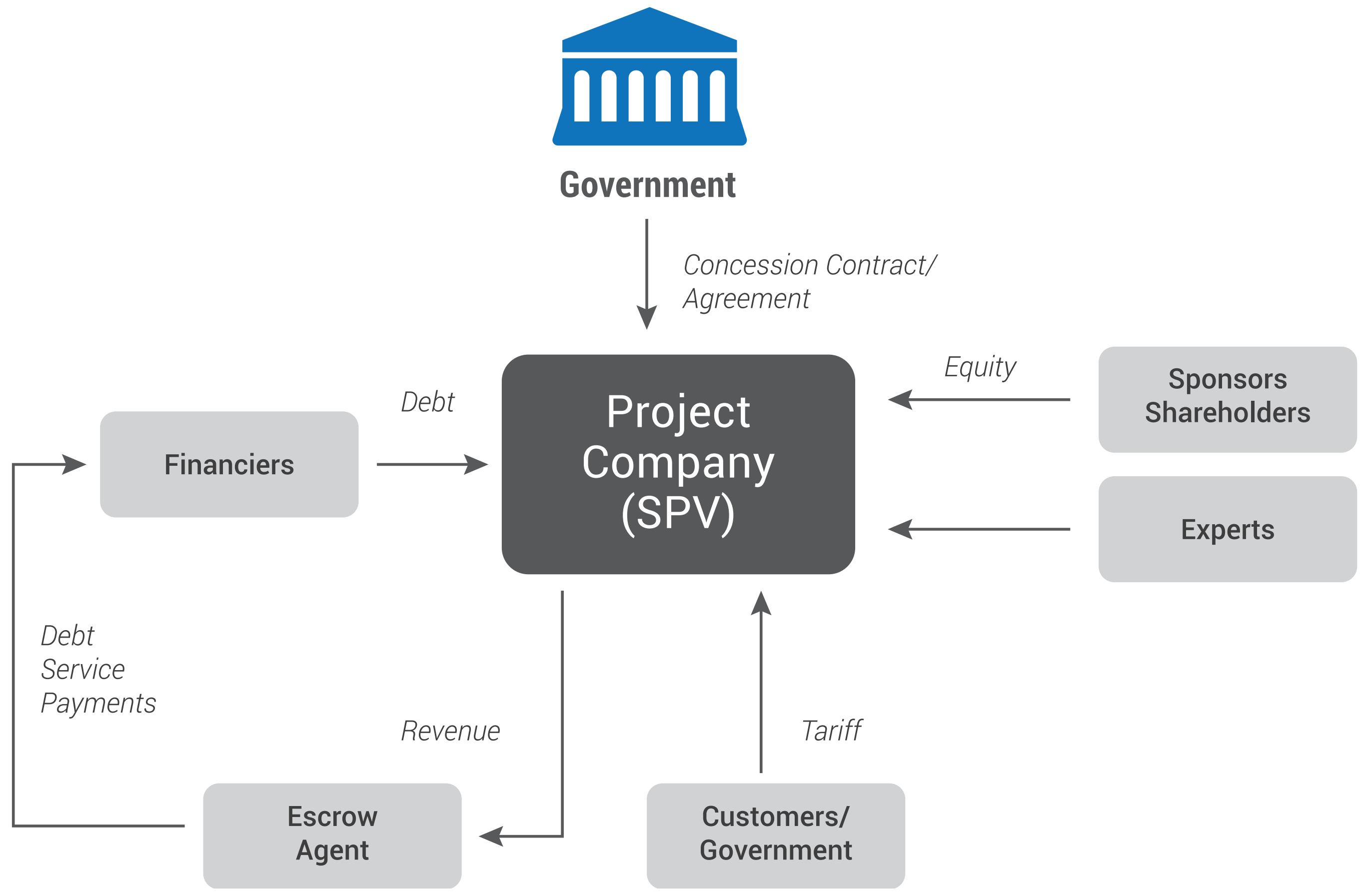
1.5 Typical PPP project structure

In a classic PPP project various parties come together and work towards the same goal. These parties have different set of skills and expertise. Hence, the structure of a PPP project can be reasonably complex which involves contractual understandings with the government, project sponsor, financiers, operator, suppliers, contractors/sub-contractors, other third parties and customers.

Most PPP projects are executed through formation of a distinct commercial entity called Special Purpose Vehicle (SPV). The SPV takes form of a legal body and carries out the project. The contractual agreement with other associated parties involved in the PPP project are negotiated through this SPV. Additionally, it has been observed that an SPV is generally the preferred mode of PPP project execution in the event of limited or non-recourse situations, where the lenders rely on the project's cash flow and security over its assets as the only means to repay debts.

A simplified structure of a PPP projects is depicted in the figure 1 below. However, the actual structure of a PPP project generally depends on the form of partnership model.

Chart 1.1: Typical structure of a PPP project



Source: A Guidebook on Public-Private Partnership in Infrastructure

[4] UNESCAP – A Guidebook on PPP

2 Key Feature of Kuwait's PPP Law of 2014

Kuwait passed a new PPP law in 2014 aiming to overcome the challenges faced under the old law passed in 2008 (law no. 7) that was basically hurting the procurement for PPP projects in the country. The 2008 law was repealed by the virtue of new PPP law under article 45 passed in 2014, however, the new PPP law was not implemented until 2015 by when the law's executive regulations were published.

Potential taxation benefits under the new law include income tax holidays and exemptions from customs duties. The Law provides general guidelines with respect to the project procurement procedures, details relating to incorporation of the Project Companies as well as Consortium Companies / bidding companies and information related to investment terms and transfers of the project to the Kuwaiti government at the conclusion of the PPP[5].

2.1 Timing of the Law

At the macro level, Kuwaiti government's PPP reforms coincided with low oil revenues as oil revenues declined between 2013-2015 due to falling oil prices internationally. In response, Kuwait introduced fiscal restraint and the introduction of the new law aided in that objective.

PPP reforms will provide essential cushion to both, current economic state of affairs–by the way of limiting the spending and to private economy-by the way of attracting and opening up new avenues for investment. This will enable executing various infrastructure projects without constraining the current fiscal structure. As the PPP process gathers momentum, more private investment will be channeled into allied industries and sectors.

Table 2.1: PPP projects Sector and Year wise Kuwait

Year	Sector
May 2018	Water and Waste
May 2018	Water and Waste
March 2018	Transport
November 2017	Social & Health
August 2017	Energy, Water & Waste
November 2015	Social & health
August 2015	Energy
June 2015	Social & Health
December 2013	Energy, Water & Waste
September 2012	Social & Health

Source: Infra PPP Data base 2018

The table above displays PPP projects in Kuwait since 2012, where majority of the projects were in water treatment and energy sectors. These sectors are well suited for the PPP model, since demand for water and electricity is largely inelastic and it is expected to witness steady growth ahead[6]. On the whole, the regulatory benefit of PPP reforms would invariably contribute towards capital formation in the country along with increased spending power in the years to come.

PPP projects results in more efficient utilization of resources compared to a situation when PPP policy framework is absent. PPP projects tend to benefit a wide cross section of stakeholders including construction/ allied industries and banks that can seize funding opportunities.

[5] PwC-Kuwait Public Private Partnership Law 2015
[6] Ibid

Table 2.2: Old and New Law Key Points

Key Propositions	Old Law 2008 Highlights	New Law 2014 Highlights
Higher Committee	Earlier the higher committee was granted less decision making power.	The new authority has greater power like granting of projects on PPP basis, feasibility study, and land request among others
New Public Authority	Partnerships Technical Bureau was replaced by new authority.	Kuwait Authority for Partnership Projects (KAPP) was established with more autonomy[7]
Procurement/Dispute Resolution	Amendment in PPP laws was required and arbitration was not allowed.	Under the new law, arbitration is allowed as a dispute resolution mechanism
Project Company	Under the old law it was unclear PTB or the investor would be responsible for incorporation of project company.	Under the New law, KAPP is responsible to undertake incorporation of project company[8]

Source: Marmore Research, Al Tamimi & Co & Ashurst & Co.

2.2 Formation of Higher Committee

According to the Article 2 of the PPP Law, a Higher Committee called as "Higher Committee for Public-Private Partnerships Projects" has been established. The new Higher Committee will replace the higher committee formed under the 2008 law.

In addition to the above, the PPP Higher Committee also undertakes the powers and functions of the KAPP board of directors[9]. The Higher Committee is chaired by the Minister of Finance and consists of the following members:

- Minister of Public Works
- Commerce and Industry
- Electricity and Water
- Municipality
- Director General of the Environment Public Authority
- Director General of the authority, as member and rapporteur
- Three experienced specialists appointed by the Council of ministers from among state employees.

The higher committee will be responsible for formulating bylaws, organizing meetings, and decision making process including terminating a project in the public interest. The decisions of the higher committee will be effective upon approval by the Minister of Finance.

2.3 New Public Authority

Under the new PPP law, KAPP (Kuwait Authority for Partnership Projects) has replaced the Partnerships Technical Bureau (PTB) that was previously responsible for the implementation of PPP projects in Kuwait. The authority operates under the supervision of "Higher Committee for Public-Private Partnership Projects" and is primarily responsible for preparing PPPs and advising the Higher Committee.

The role assumed by the PPP unit that facilitates the implementation of the PPP programs varies with the needs and capacity of the government (Table 2.3). Article 6 of the new PPP law details central PPP unit's responsibilities, which includes but not limited to, assessing and completing the feasibility studies, development of mechanism for submission of initiatives, developing contract templates, preparing a guidebook for PPP projects, drafting PPP agreements and Terms of Reference, developing PPP project programs, following up on the implementation of PPP projects. Notably, with the new law, KAPP can incorporate public joint stock companies for PPP implementation, and determine the capital of such companies.

[7] Ashurst Co
[8] Al Tamimi & Co
[9] Kuwait PPP law document 2014

Table: 2.3 Different roles assumed by PPP units across the world

Country	Institutional framework	PPP unit	Policy guidance	Investment Promotion	Technical support	Capacity building	Projects approval
UK	Several central PPP unit	Infrastructure and Projects Authority	✓	✓	✓	✓	✓
South Africa	PPP Unit	National Treasury's PPP unit	✓	✓	✓		✓
South Korea	PPP Unit	PIMAC	✓	✓	✓	✓	
France	Several central PPP unit	French PPP Think Tank	✓	✓	✓		
Italy	PPP Unit	Italian PPP task force		✓	✓	✓	
Kuwait	PPP Unit	Kuwait Authority for Partnership Projects	✓	✓	✓	✓	

Source: PwC, World Bank

2.4 Project Duration

The limitation on the term of the PPP Projects has been extended to 50 years compared to 30 years in the old law. However according to the new law, projects must be transferred to Kuwaiti government at the end of the term as per the Built-Operate-Transfer model.

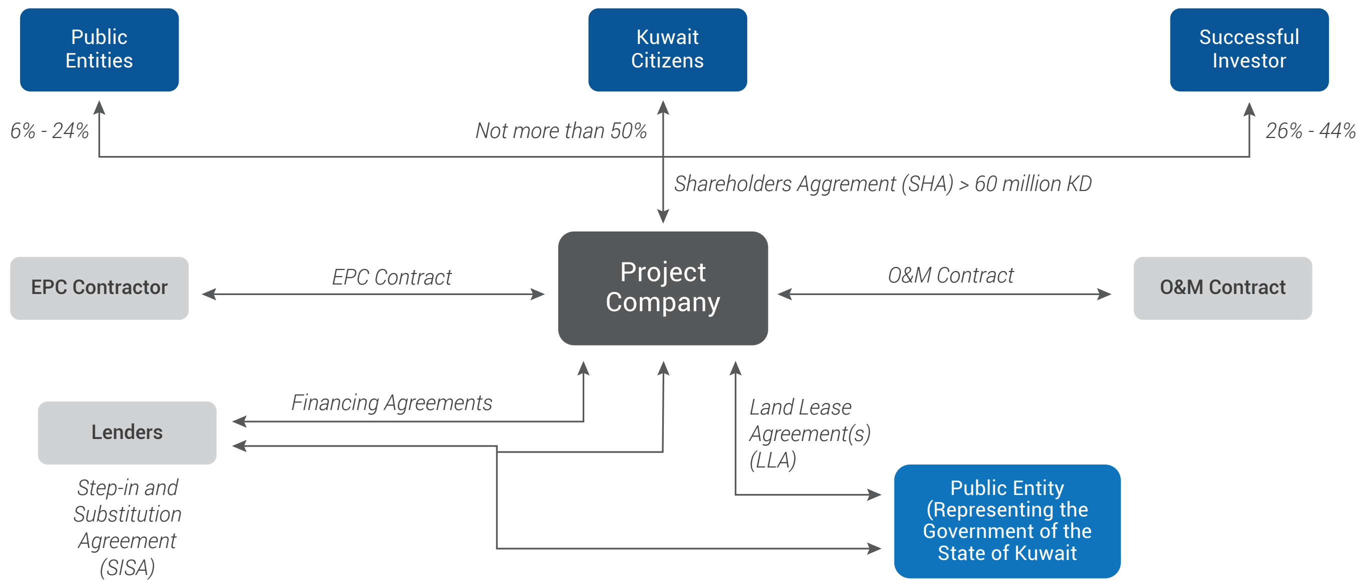
2.5 Project Company

Under the new law, the project company may be fully owned by the consortium member for any project costing less then KD 60 Mn. In case where the project value exceeds KD 60 Mn, a joint public stock company must be established. The responsibility of establishing a public joint company lies with Kuwait Authority for Partnerships Projects, where 50% of shares should be offered to public in Kuwait. The remaining 50% of shares may be split between bidding consortium and the public entity(s) or the KAPP.

Share capital will be offered as follows:

- 6% to 24% of share to be held by project entity or the KAPP until the PPP project is operational.
- 26% of shares to be held by successful investor, subject to minimum 10% allocated to the initiator
- 50% of the shares to be allocated to Kuwaiti nationals through IPO.

Chart 2.1 Contractual Legal Framework PPP law



Source: Kuwait Authority for Partnership Projects (KAPP)

2.6 Finance Ministry

The decisions made by the Higher Committee are required to be endorsed by the Finance Minister. Furthermore, the finance minister is responsible to present all the developments annually to the cabinet as a form of annual report and also forward a copy to the national assembly[10].

[10] The Law Reviews Website 2018

3 Areas of Closer Attention

With the introduction of the new PPP law in 2014, the PPP mechanism is expected to enjoy a clearer roadmap for future projects and their requirements. However PPPs' performance will be influenced by a number of other factors such as history of undertaking and executing similar projects and the extent of government intervention in awarding and financing that can impact the investors' interests.

PPP projects are generally of 4 different types, Built-Operate-Transfer (BOT), Design-Built-Operate-Transfer (DBOT), Design-Finance-Build-Operate-Transfer (DFBOT) and Build-Own-Operate-Transfer (BOOT). Some industry watchers opine that the new PPP law requires greater clarity on the various types of PPP projects, though there are specifications in terms of the mechanism to be followed for procurement and implementation of projects.

Also, the existing or continuing projects will not be impacted or affected by the new laws that have been amended in 2014. However, there is no interim legal framework for PPP projects that are already in the procurement stage but not yet signed. Essentially, according to Article 31 of the new law, PPP agreements executed shall be subject to ex ante and ex post audit by the State Audit Bureau. This may add to a layer of extended delay inadvertently in terms of quick project completion, though the audit is necessary to check for quality and factors like proper usage of resources.

4 Project financing options for PPP projects

When investors and financiers consider financing a project, they carry out extensive due diligence works in technical, financial, legal and other aspects of the PPP deal. Such due diligence assists in determining the strength of project company's (or SPV's) business plan and ascertain the company's capacity to meet objectives set out for the PPP project.

To design an appropriate financing structure for a PPP project it is imperative to conduct a cautious analysis of all alternative financial structures. The share of debt and equity in the total financing of the projects plays an important role for cash flow of the project as the expected return on equity is higher than return on debt.

4.1 Financing options

The financing for project may come from an array of sources. Often, the primary sources of funding includes equity, debt and government grants. Article 23 of the new PPP law lists the assets that the investor and project company can and cannot make use as a security

- The investor and the project company may not sell or mortgage the (state) land on which the project is located;
- The investor and the project company may mortgage and create security interest on any assets owned by the investor;
- The Investor and the project company may create security interest in favour of lenders over any amounts payable to them (i.e., proceeds) for services they provide under the PPP agreements or income earned from the project on any other aspect;
- The investor may mortgage its shares in the project company or the consortium companies to finance the project (only after the approval of the Higher Committee); and
- With the approval of the Higher Committee, the finance documents may contain terms permitting the creditors or lenders, in case of breach of the financing terms by the investor, to own the mortgaged shares or request their sale.
- The law further provides that the amount borrowed (i.e., the debt taken on) should not be more than that stipulated in the project's documents.
- Cross-border finance has been available for PPPs in Kuwait and investors have sourced funding from both international and local banks and financial institutions.

4.2 Considerations for the Cost of Capital

The cost of capital for a project is a weighted sum of the cost of debt and the cost of equity. Risk is an important element which is factored in to determine the cost of debt and equity. Lenders determine risk premiums to take into account the assessed levels of risks from various sources. These are added to risk-free rate of borrowing to determine the required return on capital. The risk-free rate of borrowing is practically the rate at which government can borrow money from the market.

Similarly, the cost of equity is defined as the risk-weighted projected return required by the investors. However, unlike debt, equity does not pay a set return to its investors. The cost of equity is therefore established by comparing the investment to other investments with similar risk profiles.

The cost of capital is often used as the discount rate, the rate at which projected cash flow is discounted to find the present value or net present value of a project. It is also important to mention here that consideration of the cost of capital is required to determine an appropriate tariff level by the government or by a regulator.

4.3 Current financing bottlenecks in Kuwait's PPP Law

As mentioned earlier, the present Kuwait's PPP Law provides limited financing options to the private sector investors as they cannot dispose or grant any lien, mortgage, or other real rights to the PPP projects. The private sector investors require to secure other collateral to raise financing.

The key financing bottlenecks can be summarized as below:

- There are limited debt financing options and local banks have been given preferences for financing such PPP projects, which results in absence of healthy competition and hence higher interest rate charged.
- The transaction for a PPP projects are stipulated to be done in Kuwaiti Dinars (KWD). Therefore, such regulations limits foreign banks to lend money which generally conduct business in USD. With such conditions, private investors have limited options to raise money from and hence are not able to strike a deal that will enable them to raise money at a competitive rate.
- There also exists "Cash trap" – due to Kuwaiti Commercial Law – which may substantially dilute the equity-IRR. Distributable cash flow is greater than net income (due to depreciation and heavy capital investment) but cannot be distributed as the Commercial Law limits dividend distribution which cannot be more than the net income.
- The PPP projects are capital intensive and are exposed to many risks; such as project delays, cost overrun, reduced revenues, etc. The Law does not provide for the step in rights of lenders in case of defaults. This limits the sources of debt financing, and substantially increases the interest cost.
- Lastly, underwriting requirements may add risk to the project and may render a project unfeasible for the private sector investors. The government should step up and underwrite for companies with good governance and stable performance.

4.4 Alternatives for easing financing bottlenecks

Development of local Capital Market for PPP projects will ease the financing burden substantially by considerably lowering the WACC (Weighted Average Cost of Capital).

Access to Debt Market will significantly reduce the cost of the PPP Project to the economy and may make some PPP Projects economically viable, which otherwise would not be.

PPP Projects can be made more attractive to Private Sector by:

- Restructuring financial guidelines for projects in coordination with investment professionals;
- Breaking down larger projects into smaller sizes or to be phased;
- Introducing Credit Ratings – rating of the project will attract funds from international institutions, and may require credit enhancements to be in place in order to improve the rating;
- Ensuring a mechanism for real risk sharing / transfer between public and private sectors;
- Having longer term concessions and more robust off take agreements.

5 Key Attributes of Successful PPPs with International Case Studies

In addition to adequate legal and institutional arrangements required for successful PPP implementation, the other critical factors include *risk allocation, VfM (Value for Money), strong private consortium, effective demand forecasts, political support and previous PPP experiences*. The following international case studies showcases some of the factors that led to the success/failure of the PPP projects.

Case study 1[11]: Over-optimistic scenarios regarding future demand can impact the PPP project

With heavy traffic volume and chronic traffic congestion in Bangkok, the government decided to develop a 30 year BOT scheme for elevated rail transit system (Bangkok's Transit System, BTS) in 1990. The SPV Bangkok Transit System Corporation (BTSC) was responsible for 100% of design, financing, construction and operation. The project company should also ensure adequate levels of safety in operations and security. The government operated on the net cost model enabling the revenue stream for BTSC to be based completely on fares. Given these provisions and projected ridership (600,000 rides per day), it was estimated that BTSC would recover its costs within the first ten years. However, the forecasted ridership was inaccurate and this led to (actual initial ridership was only 150,000) BTSC default on payment in 2002, in 2006 BTSC filed for business rehabilitation in the bankruptcy court.

Bangkok Skytrain project	
Size	$ 1.4bn
Public entity	Bangkok Metropolitan Administration (BMA)
Equity to debt ratio	2:1
SPV (Special Purpose Vehicle)	Bangkok Transit System Corporation (BTSC)
Financiers	International Finance Corporation (IFC) the Kreditanstalt für Wiederaufbau (KfW) Siam commercial bank
Shareholders	Thai Project management company (69.3%) International Infrastructure development company (8.7%) Several Thai companies (each <3%)

Though the project was successful from an operational point, it was unsuccessful for the financiers and investors. It also impacted the future mass rapid transit (MRT) projects in Bangkok, as private investors were reluctant to support demand risk in the future, this led to the government opting for gross cost model for the MRT line where the private operator's revenues are no longer linked to the actual ridership level. This also means that the operator has less incentives for increasing this level, hence finding the right balance in risk allocation will be critical for the success of PPP projects.

[11] United Nations ESCAP

Case Study 2[12]: Widespread shortcomings in the EU PPPs

The European Court of Auditors (ECA) examined 12 EU co-financed PPPs in France, Greece, Ireland and Spain in the transport and Information and Communication Technology (ICT) sector. It was found that there were considerable insufficiencies in the form of delays and cost overruns in the PPP projects. Seven out of the nine completed projects (with aggregate projects costs of 7.8 billion euro) faced delays ranging from two to 52 months and costed an additional amount of almost 1.5 billion euro in public funds to complete the project.

The failure factors reported were

- Inadequate legal and institutional framework to successfully manage the PPP projects
- The risk allocation between public and private partners was often inappropriate, incoherent and ineffective, while high remuneration rates (up to 14 %) on the private partner's risk capital did not always reflect the risks borne.
- As ICTs are subject to rapid technology changes, most of the ICT projects were not easily compatible with long contract durations.

[12] European Court of Auditors

6 Key governance principles for PPP projects

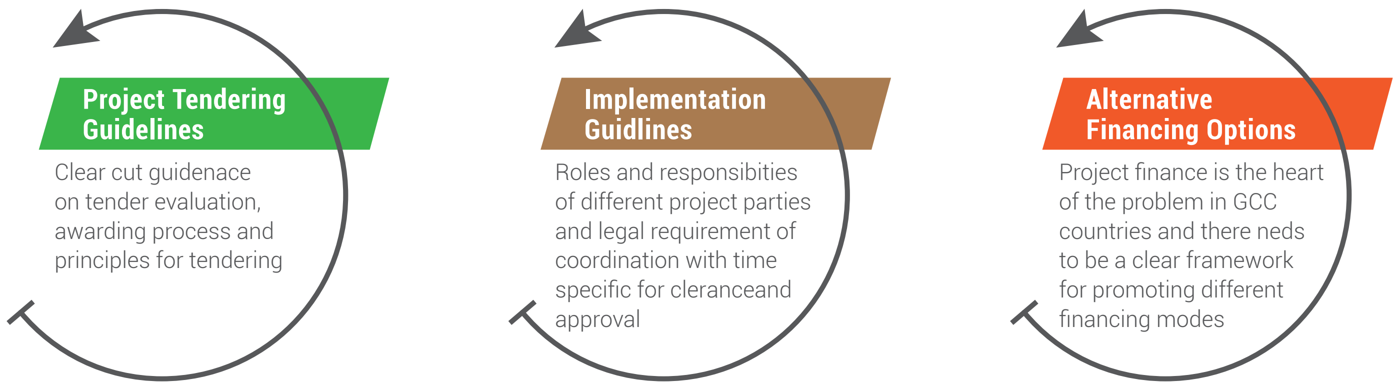
PPP projects in general faces specific challenges like transferring appropriate risks, ability to write and negotiate PPP contracts, affordability and assessing the fiscal impacts of PPPs and so on. Based on the best practices, Kuwait's PPP projects should have the following key principles:

- As KAPP is a key coordination point it should ensure active consultation and engagement with the stakeholders.
- Make PPP decision-making streamlined, fair, open and transparent, enabling faster "go / no-go" decisions;
- Free PPP from overly bureaucratic approval processes. Extensive bureaucracy and too many approvals can create major problems for sponsor agencies (and projects).
- A transparent, neutral process without any institutional, procedural bias between the regional and international players would foster competition.

The lack of government funding should not be the main criteria for implementing a PPP project as growing influence of regional capital markets might open up for other innovative methods of financing such as project bonds, sukuk issuances and export credit agency financing. Such new options can maintain spending on projects without impacting their balance sheets.

In PPP, there are additional costs - usually the cost of borrowing money is higher for the private sector than for the public sector and there are administrative costs for the management of PPP contractual regimes. Transaction costs of PPP projects can also be substantial. PPP projects may also impose many explicit and implicit liabilities on the government. OECD points that for a better governance of the PPP project a fundamental assessment of specific issues and comparative cost has to be done before the government's decision to invest. Similarly the risks that has to be retained by the public sector or transferred to the private through contract terms has to be clearly identified.

Chart 6.1:Key Elements for Mitigating Risk and Enhance Growth in PPP Domain



Source: Marmore Research and Secondary Sources

A project may not be considered for being implemented as a PPP project unless efficiency gains from improved project delivery, operation and management, and access to advanced technology can offset the above-mentioned additional costs. In fact, many countries have established value for money (VfM) as the main criterion in judging the merits of a PPP option for a project. Kuwait has a clear mandate for VfM analysis that the public entity has to carry out. Value for money analysis prepared at multiple changes of project development can widely help the governments as it serves as a decision tool to ensure that the choice of a PPP procurement alternative is the best value proposition for the public sector at a given point in time. Thus PPP requires a number of capacities in terms of both institutional structures and legal framework in the government.

7 GCC PPP Environment and Experience

In the GCC, Kuwait has been pioneering in terms of introducing PPP Laws. UAE was the second GCC Country, after Kuwait, to pass the PPP law in 2015 for the Emirate of Dubai. Saudi Arabia doesn't currently have a specific PPP law, the infrastructure projects have been undertaken in accordance with the Government Tenders and Procurement Law. The National Centre for Privatisation (established in 2017) is responsible for enabling the privatisation program in the Kingdom of Saudi Arabia. Other Gulf nations like Oman, Qatar and Bahrain doesn't have a PPP law or a central PPP unit to facilitate the implementation of the PPP programs. In the view of number of infrastructure projects being executed for the preparation of FIFA World Cup 2022, Qatar also has plans to devise formalized legislation for PPP projects. In the UAE, Dubai and Abu Dhabi both have already executed a number of successful PPP projects but these projects are governed by sectoral regulations.

GCC region follows primarily two approaches to execute large-scale PPP projects. Firstly, a formal PPP legislation overlooks activities in all sectors with clear indicatives by government (Under this type of arrangement, financing and obtaining finances later during the project are dealt under the commercial law where project companies face restriction and requirement as Non-PPP companies' face). Secondly, there is an alternative approach wherein government have delineated sector specific guidelines to execute PPP projects. For example, in Dubai the RTA has its own PPP directives to execute transportation related projects in the Emirate.

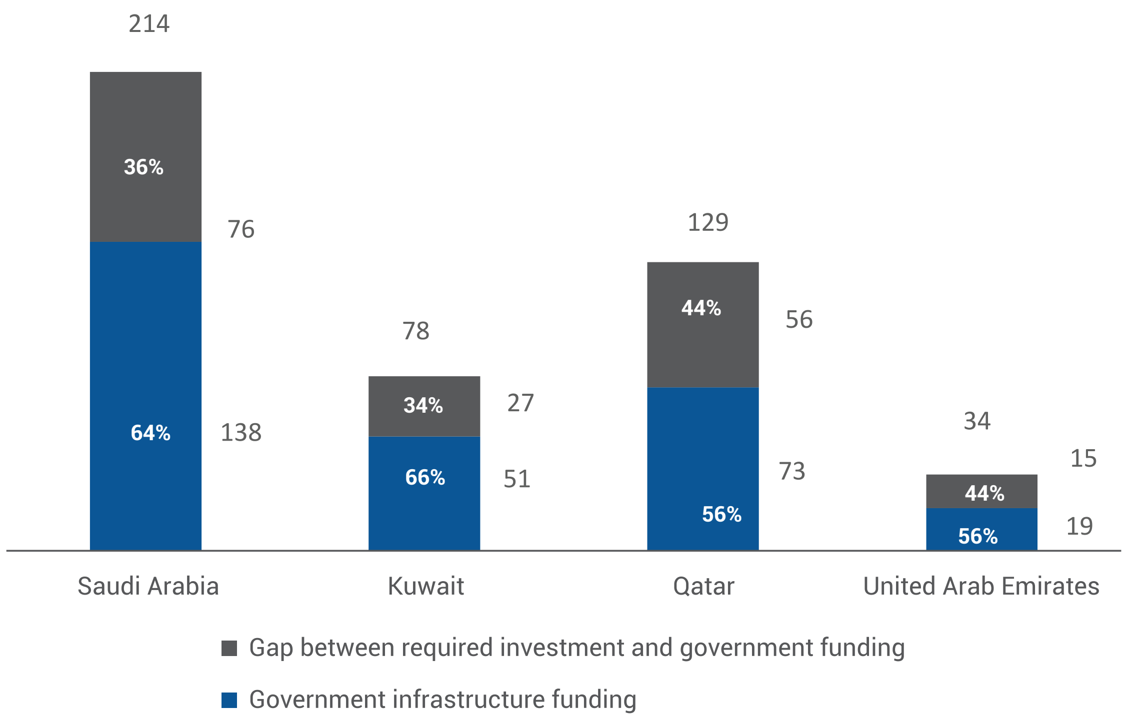
In case of the type of PPP model, Built-Operate-Transfer (BOT) is popular across various sectors in the GCC countries[14] as it would transfer the project back to the government at the end of the project term. BOT is a typical structure for project finance. Project finance is also the most popular model for finance in all the GCC countries[14]. It is the kind of financing mechanism where funding is obtained for a specific project and the company or the consortium will be repaying the loans raised on the cash flows generated by the project.

In the UAE, project finance has been used mainly in power and water sectors. However solar energy sector has also witnessed steep rise in project finance.

UAE has power and water sector specific PPP laws; otherwise project finance would have been dealt under commercial law, where it would be necessary to register the mortgage of property, land or some other immoveable property before submitting applications for the concerned project. In some cases like with the amendment of laws in Kuwait in 2014 which provides some opportunities for project companies to be financed by foreign investors because article 34 exempts the nationality requirement (51% of holding must be offered to Kuwaiti nationals) for project companies. However, this may be the strategic option for companies or consortium operating in other GCC countries.

Also tightening fiscal measures in the GCC region contributes to project delays and sometimes even cancellation. Reductions in government spending has caused a huge project funding gap in the GCC which the S&P estimates to be $270bn[15]. In addition, increasing capital requirements with Basel III implementation might likely reduce the regional banks' ability to support projects with long tenure, this would affect projects like Rail-Road construction. Mitsubishi UFJ Financial Group (MUFG) points that a project finance market of the size and scale of the Middle East requires more than just one or two big lenders like a good number of primary banks and also secondary interested parties, including debt and institutional investors for a sustainable market. Over time we might thus expect a wide range of banking institutions and a diverse array of funding sources to meet the project finance gap in the region.

Chart 7.1 Gulf infrastructure funding gap 2018-2022 (USD billion)



Source: Oliver Wyman

Shariah-compliant financing provided by Islamic banks or conventional banks through Islamic windows has become increasingly important for the project finance market in the region, particularly in Saudi Arabi[16]. Nevertheless, other financing options are still finding takers in the GCC markets mainly because laws and regulation dealing with them and PPP domain itself are still in the process of development, amendments and refinement. Hence much success has not been attained in other financing mechanisms especially in PPP area in the GCC.

On the regulatory front, back-to-back reforms in terms of contract and opportunity for arbitration (in some countries) led to the creation of a level playing field for PPP to prosper. Project arrangement between government and project companies in the GCC needs a total restructuring in such a way that the scope of financing and flexibility of operation are retained at least during the tenure of the project.

[13] Middle East Legal Report-King & Spalding-2017
[14] King & Spalding 2018

[15] The Banker
[14] Ibid

Table 7.1: GCC PPP regulatory Environment-Key Highlights

Countries	PPP laws
Saudi Arabia	Issued Draft law in 2018
Kuwait	The PPP law 2014 tend to govern the procurement of all PPP projects in the state whereas in other GCC countries power and water projects are mutually exclusive[17]
UAE	The PPP laws in place are broad and detailed. Key Highlight: No formal requirement of public offering of holding of project company as in case of Kuwait[18].
Oman	No laws announced as yet[19]
Bahrain	No Specific laws as yet
Qatar	Expected to announce soon

Source: Marmore Research & Secondary Sources

Another key dimension associated with PPP and its operation in the GCC countries is regulatory approvals, compliance and licensing. GCC countries doesn't fare well on the Global ease of Doing Business Index.

Table: 7.2: GCC Countries Doing Business Ranking- 2018

Countries	Ease of Doing Business	Starting a business	Construction Permits	Enforcing Contracts
Bahrain	66	75	47	111
Kuwait	96	149	129	73
Qatar	83	89	19	123
KSA	92	135	38	83
UAE	21	51	2	12
Oman	71	31	60	67

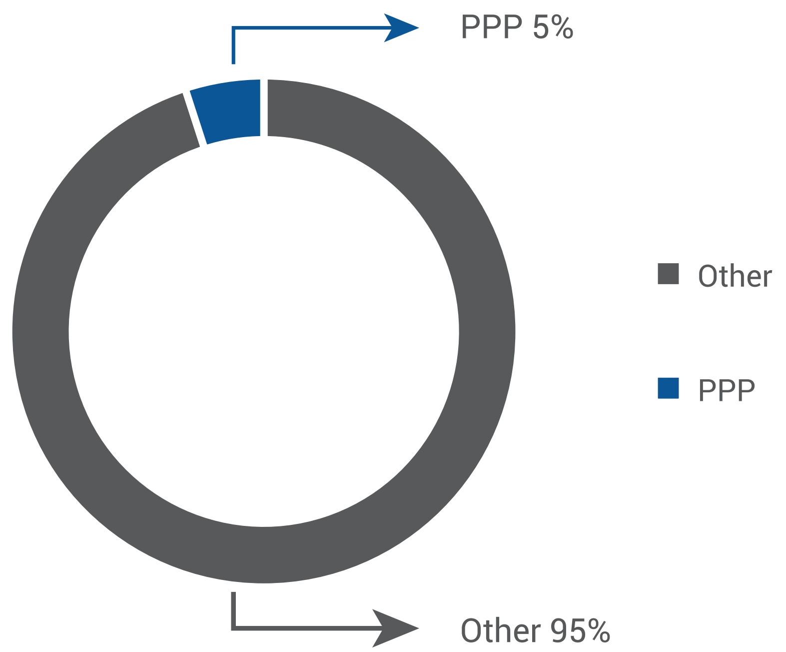
Source: Doing business 2018 report

Filing and kick-starting commercial operations in GCC countries still seems to be cumbersome process; despite constant reform drive in the recent years especially after the sustained drop in oil prices since 2014.

- Overview of PPP projects in GCC countries
  The below chart shows the proportion of projects awarded to PPP and to other means for all GCC countries for a period of 2011-2017.

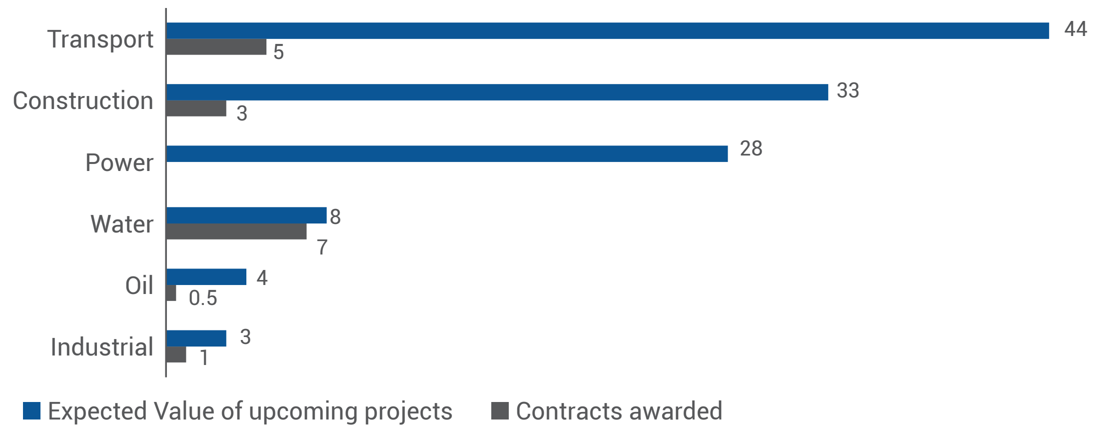
[17] Ibid
[18] Norton Rose Full Bright Website 2018
[19] Construction Weekly 2018

Chart 7.2: GCC PPP Contract Awards 2011-17



Source: MEED 2018

Chart 7.3: PPP projects Value by Sector in US$ Bn



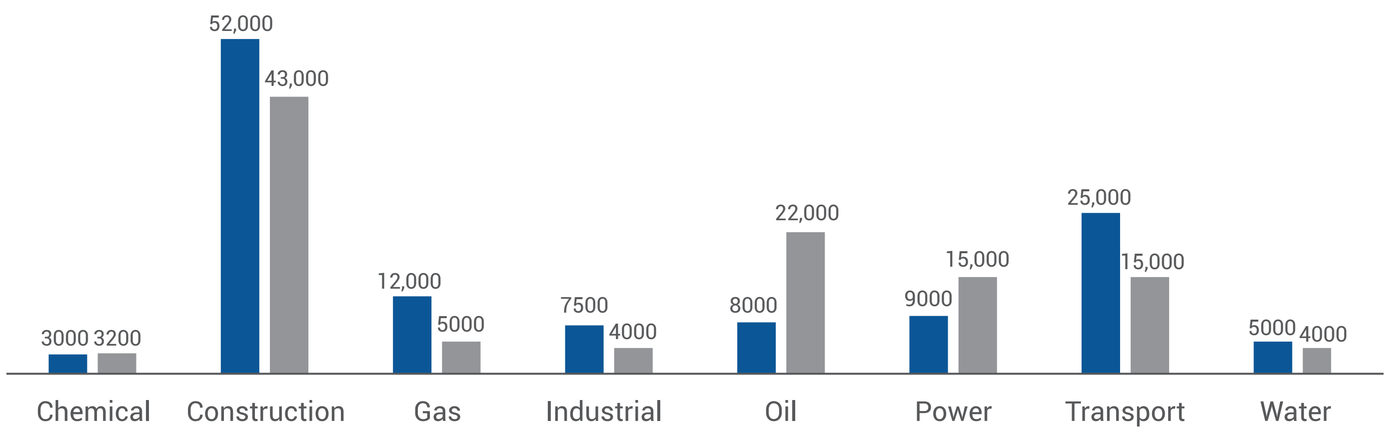
Source: MEED 2018

The chart above further elaborates the state of PPP projects in the GCC region. Transport sector bags most of the PPP projects followed by construction and utilities.

Saudi Arabia has the largest infrastructure projects' pipeline in the region (PPP projects worth USD 42.9bn planned[20]). With its successful PPP track record in power generation and airport sectors, the country has built substantial momentum for PPP. It is already working on PPP arrangements in other core infrastructure sectors including water management, whereby management contracts for 16 cities will be awarded soon.

Qatar has a $150 billion infrastructure spending plan focused on large scale transportation and sports infrastructure projects[21]. Furthermore, funding is expected to be slightly easier to source as we look at the requirements to seek returns for investors from a macro perspective – with central banks reigning in QE and returns getting lower and lower on high grade government bonds[22].

Chart 7.4: PPP deals in GCC countries in US$ bn by sector 2016-2017



Source: MEED Insights, August 2017

Table 7.3: Expected Number of PPP Projects in GCC by sector

Sector	Number of Projects	Value in US$ Bn
Saudi Arabia	15	17.5
Qatar	NA	NA
Bahrain	9	20.6
UAE	13	27.6
Kuwait	17	44.4
Oman	11	2

Source: Saudi Gazette August 2017

[20] MEED 2017
[21] Public Private Partnership-State of Qatar Document
[22] Faithful Gould website- 2018

In the GCC, the UAE and Saudi Arabia are the biggest PPP markets as a result of substantial investments being made by the private investors in power and desalination plants across the countries. With Saudi Arabia on the verge of announcing new laws, the PPP sector is set to experience massive growth. The potential sector would be rail road, power, aviation and airports, healthcare and education, transport sector with the inception of program to build new city by Saudi Arabia, PPP is at the crossroads of high growth momentum.

In projects related to port development, social infrastructure, management contracts mode will be preferred for diffusing the project and in sectors such as power, utilities, rail-road Build-operate-transfer, Build-Operate-Own-Transfer, and Build-Operate-Own models are expected to see considerable preference[23].

The first ever PPP project in GCC was launched in 1994 in Oman with Al-Manah independent power project (IPP). However, the real potential of PPP was realized when Abu Dhabi Water & Electricity Authority (Adwea) project was launched in 1998. The Adwea model had a profound impact on the GCC utility sector, becoming the template for private power. Oman re-launched its own utility privatization program in 1999 and was followed in 2000 by Qatar and in 2003 by both Bahrain and Saudi Arabia.

Evolution and transition of PPP's in GCC regions have different stories and analogies. Firstly critics of PPP model claim that GCC countries to some extent are not technically ready to subsume the mammoth scale of PPP operations mainly due to financing and operational glitches. However it has been noted that PPP strategy implemented in GCC countries is in line with the economic needs of the respective countries. Over the years since 2013-14, oscillating oil prices and recent big plunge registered in it promoted the idea of economic diversification and greater reliance on non-oil private economy. The PPP mechanism is in fact the cost-saving apparatus for the fiscally bounded GCC budgets because its saves outright capital expenditure.

[23] Public Private Partnership-State of Qatar Document

8 Outlook

The PTB (KAPP's predecessor) had earlier developed a roadmap highlighting top-priority projects within the sectors most amenable for PPPs[24]. A total of eight sectors were identified as key sectors for increasing economic diversification and private sector participation, namely: Communication; Education; Healthcare; Power; Real Estate; Solid Waste Management, Transportation and Water/ Wastewater sectors. KAPP has streamlined the list further: Education; Real Estate; Transportation; Water Desalination; and Waste Treatment.

Since 2015 (after 2014 oil price collapse) the process of fiscal consolidation, reduction of foreign labour dependence, introduction of new and robust policies for business and technology augmentation, various regulatory approvals for the promotion of trade among other have been set in rapid motion. Hence over the years PPP poised a strategic place in GCC countries and it is expected to witness substantial growth in the years ahead. The changing economic landscape and potential vast benefits along with massive infrastructure development plans in the GCC countries has placed PPP at the center of attraction for investors, banking industry, developers, technology consulting firms and government.

With respect to Kuwait's forward path in PPPs, the government is also expecting the private sector to play a bigger part in infrastructure projects, transitioning their role from construction services to partnering in key infrastructure initiatives. In addition, the expected increase in capital expenditure allocation for infrastructure projects (under the draft budget, approved by cabinet in January 2018) will promote economic development. By leveraging the private sector's technical expertise, private players can enhance the performance of key public infrastructure. The private sector involvement will also be crucial in reducing Kuwaiti government's infrastructure funding gap, which is projected to reach USD 27 billion over the next five years[25].

KAPP has seen through the successful completion of the Az-Zour North Independent Water and Power Project (Phase 1). The Project involves the development, design, engineering, construction, operation, maintenance and transfer of a power and desalination plant with a capacity of at least 1,500 Megawatt and 102 Million Imperial Gallons per Day.

The aim of delivering improved services and better value for resources spent, mainly via appropriate risk transfer, innovation, better asset utilization, etc., underpins much of PPP usage across the world. Using the new PPP framework, Kuwait is in a better position to use enhanced PPP financing approaches and procurement processes. It is notable that wherever private sector contribution to public infrastructure can deliver better value for funds, a consistent framework will help in identifying and utilizing them.

[24] Ibid
[25] Oliver Wyman

9 Appendix

List of PPP Projects in Kuwait and Key features

1. Az-Zour North IWPP Phase 1

Sector	Power
Stage	Completed
Model	BOT
Finance Type	Project finance
SPV	Shamal Az-Zour Al-Oula
Value	USD 1,799.98m
Debt($1.4bn)	Bank of Tokyo-Mitsubishi UFJ, Sumitomo Mitsui Banking Corporation, Standard Chartered Bank, National Bank of Kuwait and Japan Bank for International Cooperation
Equity($366m)	Electrabel S.A. (17.5%), Sumitomo Corp (17.5%), AH Al Sagar & Brothers (5%), Partnerships Technical Bureau (50%), KIA (5%) and Public Institution for Social Security (5%)
Financial Advisor	BNP Paribas
Technical Advisor	Lahmeyer International
Legal Advisor	Chadbourne & Parke, Allen & Overy, Latham & Watkins, Al Tamimi, Clifford Chance, and International Legal Group

2. Umm AlHayman WWTP

Sector	Water Management
Stage	Tendering
Finance Type	Project finance
Model	DBFMO
Project Consortium	WTE Wassertechnik and International Finance Advisors K.S.C.C
Estimated Value	$2,000m
Financial Advisor	HSBC
Technical Advisor	Fichtner
Legal Advisor	Norton Rose Fulbright
Contract Length	25 years

3. Kabd Municipal Solid Waste Treatment Facility

Sector	Waste Management
Stage	Tendering
Finance Type	Project finance
Model	DBFMO
Project Consortium	Constructions Industrielles de la Méditerranée (CNIM), Gulf Investment Corporation(GIC), and Al Mulla Group Holding Co (AMG)
Financial Advisor	PwC
Technical Advisor	Fichtner
Legal Advisor	Ashurst
Contract Length	25 years

4. Kuwait Schools Development Program PPP

Sector	Education
Stage	Tendering
Finance Type	Project finance
Model	DBFOM
Bidders	Alargan International Real Estate Morganti Group National Industries Group Privatization Holding Company - PHC Consolidated Construction Company
Financial Advisor	PwC
Technical Advisor	Mott MacDonald
Legal Advisor	Eversheds Sutherland
Contract Length	25 years

5. AlKhairan IWPP (Phase I)

Sector	Power
Stage	Tendering
Finance Type	Project Finance
Model	DBFOT
Financial Advisor	BNP Paribas
Technical Advisor	Lahmeyer International
Legal Advisor	Covington & Burling

6. Kuwait National Rail Road (KNRR)

Sector	Transport
Stage	Pre-tendering
Finance Type	Project finance
Model	DBFMO
Estimated Value	$10,000m
Contract Length	30 Years
Project Consortium	DBFMO

7. Rest Houses And Doha Chalet's Service Centers

Sector	Real Estate development
Stage	Pre-tendering
Model	BOT
Contract Length	22 years

8. Al Abdaliyah ISCC Plant

Sector	Power
Finance Type	Project finance
Model	BOT
Estimated Value	$3,091.96m
Contract Length	25 years

9. Az Zour North IWPP Phase 2 &3

Sector	Power
Stage	Tendering
Model	DBFMO
Finance Type	Project finance

10. South Al-Jahra Labor City

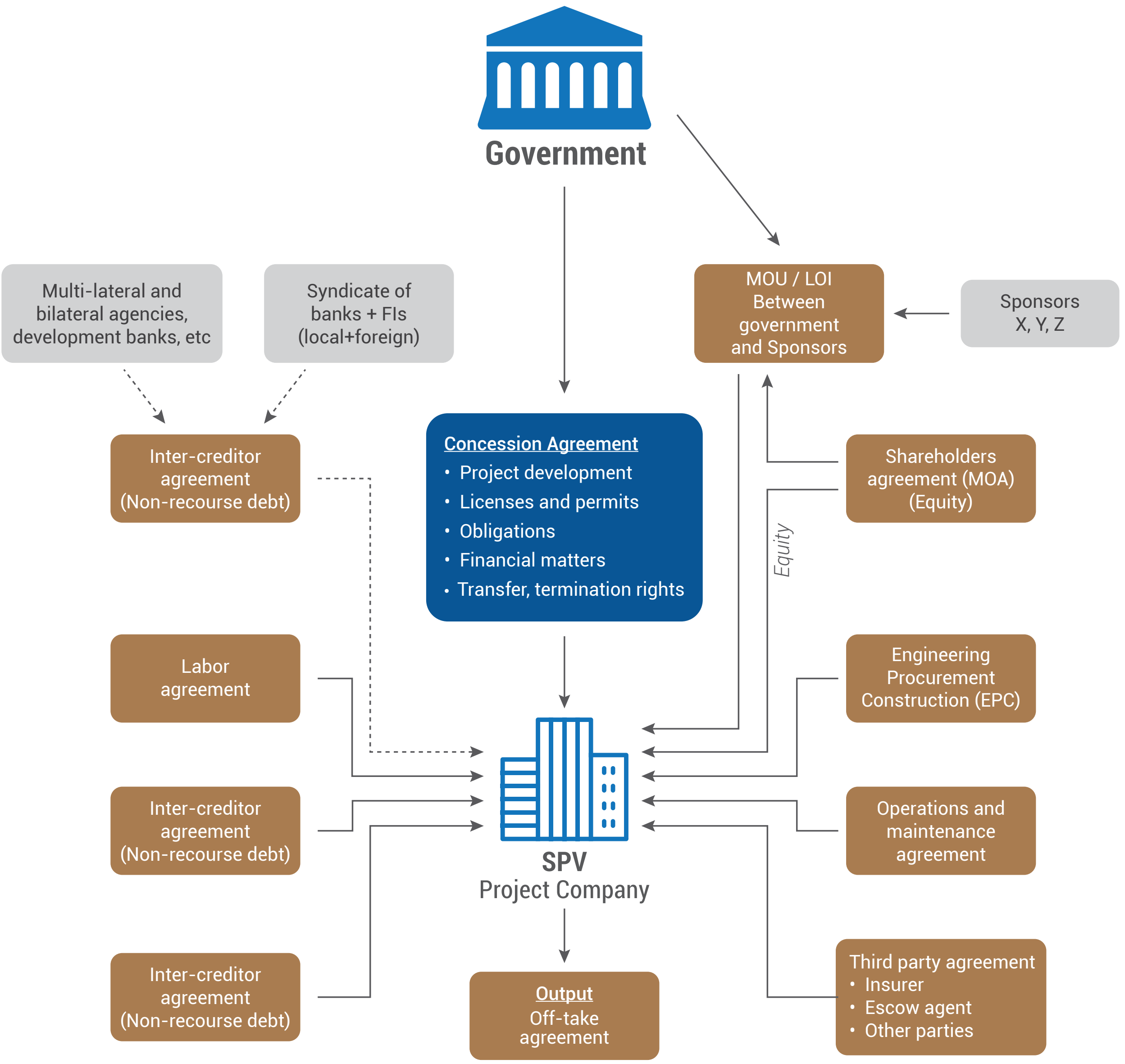
Sector	Real estate
Stage	Pre-tendering
Model	DBFOM
Project duration	40 years

11. Egaila Services and Entertainment Center

Sector	Real Estate
Stage	Tendering
Model	DBFOM
Contract Length	27 Years

Source: IJ Global, Kuwait Authority for Partnership Agreement (KAPP), various GCC media sources

Appendix 2: Agreements in a typical PPP arrangement



------→ Improvement needed for Kuwait PPP

Source: A Guidebook on Public-Private Partnership in Infrastructure

About marmore

Our vision

To be the first choice for obtaining strategic intelligence on the MENA region.

Our mission

Serving businesses and institutions with reliable information and intelligence about MENA, needed to catalyse growth, understand the larger environment and facilitate decision-making

Our aim

Advocate intellectual research on MENA economics, businesses and financial markets and provide customized, actionable solutions.

Our foundation

- A subsidiary of Markaz: Investment bank and asset management firm with 40+ years of history
- Markaz research activities commenced in 2006
- Marmore established in 2010 to intensify the research activities
- Publishes research reports and provides consultiong services

Published research

Industry research

Marmore's industry reports provide information on industry structure, key players, market analysis, demand drivers, competitive analysis and regulatory requirements.

Economic research

These reports are produced as thematic discussions based on current issues in the economy. The reports aid key stakeholders such as investors, businessmen, market participants, and policy makers in understanding the impact of a particular theme on the economy.

Infrastructure research

Infrastructure research highlights bottlenecks in the sector and areas requiring urgent investments. Our infrastructure report analyses the link between economic development and infrastructure and showcases supply & demand challenges in the GCC and investment opportunities.

Capital market research

Capital market reports provide an analysis of stock & bond markets in the MENA region including outlook. These reports are strategic in nature and provides investment perspective to readers.

Policy research

Marmore has partnered with several leading thought leaders and institutions of repute to generate economic policy research studies in key areas like energy, labor, economic structure and public sector.

Periodic research

Our periodic reports capture GCC stock markets' earnings, risk premium studies, and economic development & outlook.

Regulatory research

Our regulatory research series is an effective consolidation, analysis and summary of key business, economic, and market regulations that impact business environment.

Consulting services

Marmore provides customized consulting services based on specific requirements of our clients. Marmore's bespoke consulting services marries the challenges of cost, time, scope and data availability to generate actionable outcomes that are specific to our clients' needs.

What type of consulting services we provide?

- Industry market assessment (market size, competitors, regulations)
- White label reports (industry reports, company newsletters, periodic research)
- Databases (competitors' information, target clients insights)
- Company valuation (buy/sell side advisory)
- Due diligence / Business evaluation
- Feasibility studies (market and financial)
- Business plans
- C-Suite support to leaders with intellectual, industry related needs

How do we execute consulting engagement?

Our seven step process to execute consulting engagements:

- Step 1: Requirement and scope analysis
- Step 2: Proposal submission
- Step 3: Project initiation
- Step 4: Fieldwork / research
- Step 5: Analysis & reporting
- Step 6: Review & approval
- Step 7: Report submission / presentation