

## Foundations for Public-Private Partnerships

*Josef Ernstberger, Consultant*

### SYNOPSIS

**G**overnments and bilateral and multilateral development agencies are engaging the private sector to deliver a range of services traditionally delivered by the public sector. Such PPPs involve new arrangements under which governments obtain services through contracts with direct payments or various forms of subsidization. PPPs are also increasingly valued as a means of unleashing the private sector's capacity to generate innovation in the rural sector. This note discusses the opportunities and constraints of PPPs, including their institutional settings, the capacities and skills on both sides, partnership arrangements (especially the need for contracts that clearly define outcomes and ensure accountability), and the need for independent supervision and monitoring of PPPs.

### BACKGROUND AND CONTEXT

Public-private partnerships (PPPs) bring the complementary skills of the public and private sectors to a program or project in which each partner has a different level of involvement and responsibility, with the objective of providing public goods or services. These partnerships leverage the strength and reflect the interests of the individual partners. These partnerships are not intended primarily for business development, for which business development programs are a better alternative, but for bringing about a public good outcome in partnership with the private sector. The public sector is interested in cooperating with the private sector to use technologies, capital, and know-how and (ideally) to benefit from the comparatively greater flexibility, innovative capacity, and efficiency of private companies. For the private partners, the incentive is generally that the collaboration opens an interesting new line of business.

PPPs in agriculture mainly target opportunities for environmental, social, or equitable growth. They range in scope

from cooperating on an individual project, to generating ideas and innovations in a specific field or for a specific purpose, to major strategic alliances that address major concerns in the development of the agricultural sector.

*PPPs implemented through individual development projects* are characterized by a relatively clear and specific expected outcome or service for which the private partner provides know-how and technical solutions. In infrastructure projects this kind of arrangement is generally known as a “design-build,” “design-bid-build,” or “design-build-operate” contractual arrangement. For example, an IT company may be invited to develop and implement a tailored search engine for a local Internet-based agricultural extension system.

*When PPPs are used to generate ideas and innovations*, the public sector defines more or less specific fields and objectives in which it seeks progress (environmental health, social welfare, agricultural growth, and so forth) and issues a call for proposals to public and private entities, who submit their ideas for collaborative work to generate the desired innovations. The proposals are submitted for review, and if they are selected for funding, the public and private partners implement the programs.

*Strategic alliances* usually involve long-term cooperation (ten or more years), multinational companies, or groups of companies. Examples include the development and introduction of minimum social and environmental standards for agricultural or forestry products, fair trade arrangements, and similar ambitious programs.

In agriculture, PPPs are more promising in some areas than others. They can be quite effective for introducing environmental and/or social production and processing standards, which then become national and sometimes even international standards (box 5.7). Examples of collaborative projects that subsequently resulted in national legislation include projects on standards for organic and fair trade food production, control of child labor, and the protection of forest biodiversity.

### Box 5.7 A Public-Private Partnership to Implement Labor Standards in Asia

Many international companies produce goods in developing countries where international labor standards are not followed and in any case are challenging to monitor. A public-private partnership run by GIZ and Tchibo GmbH engages workers in factories in Bangladesh, China, and Thailand in implementing the International Labour Organization's core labor standards and improving working conditions. Since the project started, 13 local training providers have acquired the specialized knowledge and tools to advise suppliers on setting up company structures for dialogue and implementing social standards. Forty firms are taking part in the pilot, and the number is rising. All have designed and implemented action plans, including plans for electing staff representatives, avoiding forced labor, and reducing overtime.

Source: GIZ 2009.

Note: GIZ = Deutsche Gesellschaft für Internationale Zusammenarbeit.

PPPs have also helped governments or development organizations direct innovation toward specific areas of public interest. Governments or development organizations either acquire innovations directly from the private sector or, through competitive research grant schemes or idea competitions, challenge the private sector to pursue innovative ideas and technologies of public interest. Efforts could be as specific as identifying a solution to a particular plant disease or as general as improving energy use in agricultural production systems. (See table 5.1 in the module overview; see also module 4, IAPs 2 and 3, for examples from India and Chile.)

A number of countries have started to use private organizations or NGOs to provide specialized services (such as agricultural advisory services) that public agencies once provided. Development organizations have turned to commercial or noncommercial NGOs to deliver extension or training to farmers or train cooperatives and agricultural processors. For more detail, see module 3.

With technologies and production processes becoming more complex and technically demanding, governments increasingly use private sector capacity for regulatory controls and enforcement. Partnerships have been formed with leading enterprises or specialized private companies and

laboratories to regulate biosafety hazards, control animal diseases, detect genetically modified ingredients in food, and enforce restrictions on seed imports or exports, among other activities.

### IMPLEMENTATION ARRANGEMENTS AND INVESTMENT NEEDED

Countries require a *governance framework* that brings together the capacities for designing and executing PPPs. In most countries, line ministries or lower-level government institutions execute PPPs, which may require public officials to master new skills. They must know how the private sector operates and design collaborative programs accordingly. They must assess the risks and incentives that make collaboration attractive and do not waste taxpayers' money. They need skills to negotiate and manage contracts, and to avoid disturbing markets, they need to be able to assess the long-term implications of their partnership programs for industry structure and competitiveness. A new way to provide these capacities is to establish PPP units within cross-sectoral ministries such as finance or planning (Dutz et al. 2006). These units can operate in several ways. For example, they can provide information and guidance to other government departments for designing and preparing PPPs, provide advisory support and funding to line departments or agencies, or directly approve PPPs.

The *execution of PPPs entails numerous steps*, beginning with the selection of private sector partners. For most PPPs, specially convened committees—whose membership comes from government and the private sector but should not be dominated by the government representatives—select the private partners. Depending on the nature of the partnership envisaged, the committee may also include farmers or representatives of farmer organizations, agricultural education, extension, or NGOs. Competitive application and selection procedures are common. The objectives of the partnership program, the conditions for application, and the funding arrangements are publicly advertised. One or more rounds of proposals follow. In evaluating proposals, the selection committee often calls upon additional expertise in the form of a technical expert group or individual experts. These experts might prepare a short list of candidates, but the final decision remains with the committee. After selecting the private and public partners, it is a good practice to formalize the partnership through a contract or signed memorandum of understanding.

Generally PPPs are *managed by project implementation units* established for this purpose and supported by a

secretariat with appropriate technical and administrative capabilities. Every PPP also requires a framework for M&E to ensure that the program is on track and make adjustments as needed. It is vital for the partners to agree beforehand on the M&E framework and the practical arrangements for implementing it. The framework must be flexible enough to handle an unpredictable timeframe and outcomes, given that many of the key variables will have a significant amount of uncertainty. An independent but mutually accepted monitoring agency or organization should implement the framework.

Particularly in the agricultural sector, PPPs require *supplementary funding to build capacity in most or all private partners*. Capacity building can extend from the application process to proposal development and program implementation.

## POTENTIAL BENEFITS

As mentioned, the major benefits of PPPs derive from using the complementary strengths of the public and private partners to:

- **Attain efficiency gains.** Many public goods can be delivered by private partners more cost-effectively, especially if contracts are output oriented and give the private partners the flexibility to identify the most cost-effective technical solutions.
- **Mobilize resources and investments.** PPPs have significant potential to mobilize additional resources and funding. Sometimes only limited or even no public funds are needed to trigger significant private investment (box 5.8; IAP 3).
- **Develop innovative solutions.** PPPs can encourage the private sector to come forward with creative ideas.
- **Reduce risk.** Transferring part of the project risk to private partners can be one of the key benefits of PPPs and result in better control over public spending, the service delivery time frame, and quality of service. Output- or delivery-based payments can be effective for reducing risks.

## POLICY ISSUES

PPPs often require the public and private sector to *redefine their respective roles and responsibilities*. This issue requires particular attention from policy makers. Many governments already find it difficult to separate the functions of the two sectors; they may subsidize private enterprises without clear justification or operate what appear to be commercial agri-

cultural ventures such as plantations or seed companies. For these reasons, PPPs can aggravate rather than resolve uncertainty over what each sector should properly do.

Many PPPs also suffer from a *lack of suitable public institutions and legislative arrangements*. Donor programs often bridge this gap by setting up their own program- or project-specific implementation units and operational manuals. While project-specific arrangements may be necessary, as long as an overall institutional and legislative framework is lacking, it will be challenging to implement PPPs as a regular feature of government procedures and programs.

As discussed, poorly designed PPPs can easily *distort markets*, and many PPPs probably do so. Major market distortion occurs when public funds are invested in activities that the private sector would pursue in any case (crowding out private investment) or when private companies participating in PPPs achieve an unfair and unjustified market or production advantage over their competitors.

To attract public investment, private companies tend to emphasize their social or environmental responsibility, but their ultimate (and legitimate) interest is to generate revenue. PPPs will remain *sustainable* and private partners will meet their obligations in the long run only if this interest is appropriately factored into partnership arrangements acceptable to all participants. The simplest PPPs use public funds to pay private enterprises to deliver public goods. More complex arrangements pay for the delivery of public goods by incorporating the price of the public goods (such as social or environmental services) into output prices.

Although PPPs can reduce the gap between technology development and adoption and make public research institutions more effective, responsive, and demand driven, they do have risks. Private interests can supersede public interests in public research agendas. Governments can *lose the public research capacity* that is critical for developing technologies that may not be commercially attractive but are in the public interest.

## LESSONS LEARNED

The experience with PPPs can be distilled into guiding principles to help practitioners develop and invest in partnerships while avoiding problems such as market distortion and poor sustainability. Over the years, important lessons have been learned about which private enterprises and farmer organizations make successful partners for the public sector and which strategies work best for selecting them. Issues related to contracts, the partnership's time frame, the

## Box 5.8 A Public-Private Partnership to Conserve Genetic Resources in China

The Chinese government maintains important genetic stocks for animal breeding at a number of stations throughout the country. In Anhui Province, the government contracted a medium-scale company engaged in pig breeding and processing to protect an endangered pig variety called Wei Pig, which was close to extinction. The company undertook to commercialize the variety as a niche product while continuing with its mainstream pig production business. The market strategy for Wei pig involved a special “near nature” production process, in which poor, small-scale farmers in mountainous areas raised pigs under contract for the company, which operates a breeding center that also functions as a park

Source: Author.

for visitors. The higher prices of meat from these pigs compared to conventionally produced pigs reflect the higher costs of the more environmentally and socially oriented process used to produce them. The government provided a share of the initial financing for the company and its contract farmers. This partnership made it possible to close a government facility and sustainably protect genetic resources without public funding, once the cofinancing ended. The partnership succeeded owing to a combination of private technical know-how and experience, an innovative business and marketing concept, and significant private financial resources, complemented by public startup funds.

capacity gaps that may need to be filled, and arrangements for M&E are also important to consider before the partnership begins. Details of these guidelines, lessons, and issues follow.

### Guiding principles for partnership

Guiding principles for PPPs involve the clarity of their political objectives, potential mutual benefits, additionality, competition and transparency, and sharing of risks and responsibilities:

- **Consistency with political objectives.** The public partner must clearly define the larger political objective that motivates the partnership. For example, government may want to stimulate agricultural growth as an instrument to address rural poverty and reduce increasing income disparities in a society (equitable growth). It may want to protect specific natural resources and future livelihood systems (such as forest products for traditional medicine), support specific vulnerable groups (by improving labor conditions, promoting pro-poor growth, or improving gender equity). It may want to bolster national food security.
- **Mutual benefits.** As discussed, all partners must benefit sufficiently from the partnership to honor their commitments for as long as required. The public sector benefits if the PPP proves to be effective and efficient at generating the desired public goods. Benefits to the private sector can be indirect (for example, its participation will

improve its reputation by demonstrating social or environmental responsibility), but in most cases the desired benefits are legitimate financial profits. It is important to understand the benefits required by all partners to prevent the partnership from being abused. For example, the real incentive for private partners may be to gain closer ties to government to pursue a hidden agenda such as influencing political decisions or obtaining an unfair advantage over competitors.

- **Additionality.** Public funds should support PPPs only when the private sector would not undertake a similar activity to achieve the same outcome, either on its own or as required by law.
- **Competition and transparency.** Like other forms of public investment, PPPs must give all competent private partners an equal opportunity to compete for the business opportunities supported. Setting priorities for funding, selecting partners and programs, allocating resources to partnerships, implementing and monitoring partnership programs, and all other decisions must be transparent.
- **Sharing risks and responsibilities.** In PPPs the commitment of partners is generally demonstrated by an appropriate sharing of risk and responsibilities. A major difference between PPPs and traditional public contracts such as infrastructure contracts is that the participating private companies contribute financial and/or human resources (for example, through cofinancing, matching funds, and other arrangements).

## Selecting the right partners with the right capacity

The financial and managerial strength and experience of private partners are important for the success of partnerships. As mentioned in the module overview, PPPs have to be clearly distinguished from programs to support SMEs: SME development focuses on the enterprises themselves by helping them to become fully established or providing venture capital, but PPPs focus on achieving public good outcomes. Partnerships with financially strong, experienced companies are more likely to succeed in delivering those public good outcomes efficiently and reliably. As discussed in the module overview, properly constructed PPPs do not support weak business with lucrative public contracts; nor do they weaken the public sector's or donor agency's focus on poverty. These problems can be avoided if the public sector performs due diligence and thoroughly assesses prospective partners beforehand on the basis of minimum criteria related to their financial strength, management capacity, and demonstrated ability to deliver the kinds of public goods required.

Farmers can be effective partners in PPPs and improve their impact in rural communities, yet very few farmers have the capacity to perform in PPPs without some form of assistance. Most PPPs involving farmers have a strong component for organizing farmers and providing the skills they need to perform their role in the partnership. Partnerships with farmer organizations work best when the organizations have a clear and narrow interest or focus. For example, water user associations have become strong public partners in many countries and have successfully assumed traditional public service functions. Farmer-managed grazing associations or other natural resource management organizations have successfully regulated access to and use of common resources.

Farmer organizations are increasingly important commercial partners, given that the most efficient agricultural value chains emanate from a strong, organized producer community. Forming these organizations will help to balance the power among the partners and is practically the only feasible way for government and companies to interact with producers, because organization substantially reduces the cost of interacting with large numbers of smallholders.

## Preparing the way for successful partnerships

The administrative steps in selecting partners and implementing programs were discussed earlier. The next points describe practical steps to lay the groundwork for successful partnerships.

- *For PPPs, the public good outcome is the primary objective, and it must be clearly defined* (an innovation, an environmental or social service, the performance of a traditional public service by a private partner, and so on). Confused objectives are a common defect of many programs, which fail to clarify whether their primary objective is to support or develop businesses or to deliver specific public goods.
- *Clearly define the criteria that a private partner must meet to participate*, especially the type of partner (private company, farmer group, and so on), legal status (perhaps farmer organizations must incorporate to participate), size, previous experience, and technical, financial, and managerial capacity.
- *Clearly specify the contribution expected from each partner*. Contributions can take many forms: financial resources, human resources, risk-sharing arrangements, sharing of innovations, or access to confidential or internal information (financial data, income, cash flow, technical processes). It is rarely in the interest of companies to share information related to innovative technologies, business concepts, or financial status, but if this information is necessary to achieve the partnership's objectives, this requirement must be very clear before potential partners apply for funds. This point reinforces the earlier point that absolute clarity at the outset can prevent conflicts from derailing a partnership.
- *Provide transparent information on modes of public financing and decision making*. Information about the size of and conditions for public financing is generally straightforward. The problem lies more with the lack of clarity over government procedures and the time they require. Private companies are especially frustrated by complex and lengthy public procurement procedures and bureaucratic clearances, but if they are aware of procedural requirements beforehand they may cope better.

## Contracts

Like any business relationship, each PPP should be based on a signed contract between the partners, usually representatives of the government partner, company, and farmer organization, as relevant). At a minimum, the contracts must:

- Define each expected outcome, the corresponding indicators (measurable and conducive to monitoring), and time-bound targets. This level of specificity may seem challenging for PPPs intended to develop innovations, because of the organic nature and unpredictability of the



process. The intended outcome is already clear, however, for specific partnerships based on a proposal to provide an innovative business idea, technology, or public good or service, and the partners need to be assessed against their progress in achieving that outcome.

- Specify the resources committed by the partners, along with a detailed financing and implementation plan.
- Include a monitoring framework with agreements on the monitoring arrangements and contract supervision by an accepted third-party monitoring institution or individual (see the concluding part of this section).
- Define the exit strategies and follow-up arrangements (as discussed next).

### Exit strategies and sustainability

PPPs generating social or environmental goods may end once a good has been delivered, or they may need to continue for as long as the public good is required (ideally without public support). For example, if the social or environmental value of a particular good becomes a critical part of the marketing concept (as with many organic and fair trade products), the *level of commercial interest* may be sufficient for the government to withdraw public support. If the partnership pilots environmental technologies or social standards that are eventually embodied in *mandatory regulations*, they will be sustained if compliance with regulations is assured.

PPPs generating innovations require an exit strategy based on *transferring and adopting the innovation*. Many PPPs are designed to include elements of technology transfer. For example, World Bank-supported grant programs in Albania and Armenia required PPPs to earmark a certain percentage of funds for publicizing and/or transferring their innovations to farmers or small businesses. Because it is not in the interest of private companies to share innovative ideas or new technologies with potential competitors without compensation, future ownership of any innovation developed by the partners and any obligations to share information must be spelled out in the PPP design and clarified in the contract. Many arrangements have been developed to protect financial and other incentives to share technology and information.

PPPs that shift public service provision to private partners can be sustained by *institutionalizing partnership arrangements*. For example, private partners can be organized and authorized to collect user fees, which must be high enough to assure financial sustainability and/or maintain the business interest of the private partner. Many water-user

organizations have used this kind of arrangement once initial public support for their activities ends. Private food quality testing laboratories receive a fee for performing public-service functions.

### Capacity building

A precondition for involving farmers in PPPs is to form organizations and equip the members with the skills to be effective partners, as discussed earlier. Aside from needing to acquire management skills and an understanding of managerial procedures, farmer organizations may also require training related to agricultural production and processing, quality standards, participating in adaptive research, testing technology, and providing social and environmental services. The best practice for PPPs is separate supporting activities in capacity building very clearly from the actual funding of PPPs. One option, for example, would be to include capacity building as a separate component of the project.

### Monitoring and evaluation

If a PPP encompasses more than a single project, the M&E system should provide information corresponding to several levels of activity. First, at the level of *individual projects* (often called “subprojects” when they are part of a large program that funds numerous small projects), the M&E system should provide information on adherence to contractual arrangements and outcomes from each subproject. Second, at the *program level*, the M&E system should provide information on the program’s processes, outcomes, and attractiveness. Third, at the *policy level*, the M&E system should generate feedback on the program’s broad effects on economic growth (the causal link between the program and the resulting innovation and factor productivity) and wider social benefits.

**PROJECT OR SUBPROJECT LEVEL.** As mentioned, project-level M&E combines *contract supervision* as well as *outcome monitoring and evaluation*, and it should be done by an independent, third-party M&E institution that is acceptable to all partners. The basis for M&E of individual projects (subprojects) is established when partners enter the proposal development and approval process. No proposal should be approved for funding unless it possesses a set of clearly defined objectives linked to measurable and monitorable outcome indicators and time-bound targets. The indicators should distinguish between the public good objectives (such

as the provision of an environmental or social good or an innovation for scaling up) and the financial or commercial objectives (such as target figures for production, sales, or income and benefit sharing). These detailed indicators and targets are included in the contract between the individual partners. The contract also specifies detailed input and output parameters, such as the financial and other resources that the partners have each committed to provide.

**PROGRAM OR PROJECT LEVEL.** Program/project-level M&E should aggregate the achievements of individual subprojects and devote most of its attention to examining the effectiveness and efficiency of the PPP program. Many programs report outstanding achievements of individual subprojects but offer very little information, for example, on whether the program proved attractive for investors, partners, and beneficiaries; on any design flaws that emerged; or on whether investments were taken up slowly or quickly. Few programs use “with-program” and “without-program”

scenarios to assess their effectiveness, because designing control groups or control scenarios is difficult. Program M&E should also provide information on the overall use of funds, factors driving the use of funds, and mechanisms for delivering funds. All of this information will improve how similar projects are designed and implemented.

**POLICY LEVEL.** Some of the most difficult issues in monitoring and evaluating PPP programs relate to whether and to what extent a PPP program has influenced overall economic growth, whether it experienced or caused interference with other parts of the economy, what its wider social or environmental implications (positive and negative) may have been, the sustainability of its impacts, and finally the policy measures that should be taken as a consequence of these findings. The list of failed government interventions in the private sector is long, and the effects have sometimes been significant. On the other hand, sound analyses of the effects of PPPs will be invaluable for formulating policy (box 5.9).

#### Box 5.9 The Importance of Policy-Level Monitoring, Evaluation, and Analysis

The economic effects of public-private partnerships (PPPs) can be very large. For example, many governments responded to skyrocketing energy prices by launching programs to generate and support innovations in renewable energy. Some of these programs related to biofuels have had far-reaching consequences for agriculture and food production that remain controversial and are not yet completely understood. Another example of the economic effects of PPPs comes from China, where the government promoted PPPs (among many other strategies) to develop a modern dairy industry. The result was an enormous overstimulation of milk production. The subsequent collapse of the dairy market and bankruptcy of many producers was accelerated by scandals over contaminated milk but was probably inevitable, given the inappropriate level of market interference.

Most PPPs will not have such vast economic effects, because they are small and locally confined, but the positive or negative macroeconomic and policy implications even of small programs should be analyzed and understood. Policy-level M&E and analysis are

also important for determining whether PPPs are the right instruments for achieving certain objectives (for example, taxes or regulations could be used instead of PPPs to induce compliance with social or environmental goals).

Policy-level evaluations of PPPs can also determine whether more extensive policy measures might be warranted. For example, the China Agricultural Technology Transfer Project supports a number of PPPs with private companies to develop and test new technologies for manure treatment. Cattle manure treatment plants of different sizes, using different fermentation processes, are being tested in Heilongjiang Province; special technology to treat duck manure was developed in Anhui Province. Aside from introducing and testing technical solutions, partners in these projects are analyzing their commercial and financial parameters to learn, for example, how the competitiveness of the livestock industry would be influenced if manure treatment were to become mandatory. In other words, aside from stimulating technical innovation, these PPPs are preparing the ground for decisions about future policy measures.

*Source:* Author.