

handshake

IFC's quarterly journal on public-private partnerships

In this issue

mass rapid transit: A tool for urban expansion

financing: Beyond sovereign guarantees

low-income housing: Lessons from Latin America

q&a: Economist Edward Glaeser, former U.K. Secretary of State for International Development
Clare Short, Barcelona Global
CEO Mateu Hernández

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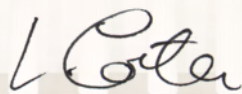
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Letter from IFC

There is a near-perfect correlation between urbanization and prosperity across nations, as pioneering urban economist Edward Glaeser points out in his myth-busting *Triumph of the City*. He reminds us that “the real city is made of flesh, not concrete,” and that cities succeed or fail due to human capital, rather than physical capital. However, the right physical capital—thoughtfully tailored infrastructure—increases the efficiency of cities, allowing for more and better innovation. Public-private partnerships (PPPs), at their best, facilitate this growth on a scale and timeline that would be impossible without private capital.

This issue of *Handshake* takes readers on a tour of urban PPPs that put citizens first. Expert authors introduce readers to solutions that have revolutionized citydwellers’ experience, like PPPs for housing, transportation, and water delivery. We focus especially on the need for a new vision of the city, featuring provocative discussions with Glaeser and with Clare Short, former U.K. Secretary of State for International Development. Glaeser reacquaints readers with the virtuous cycle created by dense urban spaces, where employers are attracted by the large pool of potential employees and workers are drawn by the abundance of potential employers. Short builds on the social benefits of this urban concentration. By pointing out that “real democracy” is based on the practice of engaging people in local development, she returns us to the certainty that cities are at the heart of civilization.



Laurence Carter, Director



Tanya Scobie Oliveira, Editor

IFC Advisory Services in Public-Private Partnerships

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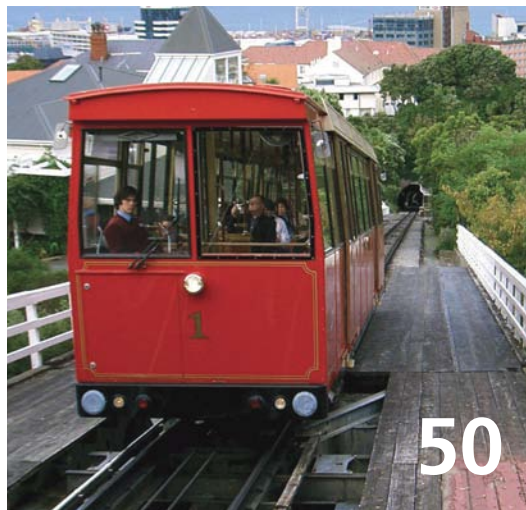
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Beyond sovereign guarantees

THE CASE FOR SUB-NATIONAL FINANCE

By Joshua Gallo & Isabel Chatterton

In many countries, central governments have devolved the responsibility of infrastructure service provision to the sub-national level, which is essential for economic growth. Along with this devolution of provision responsibility comes the requirement to raise revenues, enhance efficiencies, improve commercial viability, and reduce a dependence on external financial support—including central government guarantees.

However, central governments are increasingly unwilling or unable (due to limitations of fiscal space) to guarantee sub-national borrowings. This new paradigm is testing the sub-nationals' ability to raise financing to fulfill newfound responsibilities in infrastructure service provision.


Perhaps this is a blessing in disguise. Historically, easy access to sovereign guarantees has cre-

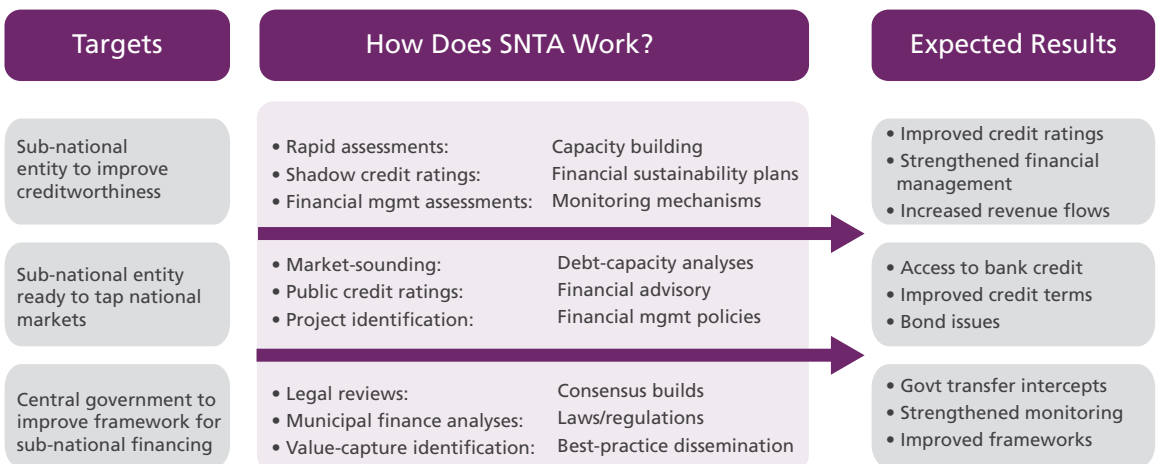
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ated perverse incentives for not pursuing more sustainable financing solutions. This dependence has also tainted the way that sub-nationals are perceived by the markets, by making them seem like reactive agents of development. This in turn has limited their access to finance and therefore their ability to develop. This approach must evolve, because whether the focus is climate change, massive migratory movements, or basic infrastructure needs, the struggle to advance the global fight against poverty and unsustainable development may be won or lost primarily at the local level in developing countries.

Change isn't easy, but rapid urbanization places growing demands on governments in the developing world to deliver essential infrastructure services to an ever-increasing number of people in cities. City budgets alone are usually unable to meet these demands, and sub-nationals' weak creditworthiness is a major constraint when it comes to raising other sources of finance. Many

cities are beginning to view the market as a potential source of much-needed infrastructure financing. To understand and weigh the various options that exist for tapping this source of finance, city officials may need specialized advice. The World Bank, in partnership with many donors, responded to this need with the creation of the Sub-National Technical Assistance (SNTA) Program.

Of course, financing without guarantees cannot guarantee access to finance. But it promises the beginning of more pragmatic and forward-looking planning at the local level; more proactive approaches to revenue raising; and a sharper focus on sound financial management practices. This enhances the ability of local government officials to meet infrastructure needs. All local governments, regardless of their size or capacity, can step forward to take on this challenge. 



The Peruvian experience

Until recently, Peruvian banks were discouraged from considering the sub-sovereign market. This was due to a lengthy and complex sub-national borrowing approval process, the limited technical and financial capacity of sub-nationals outside of Lima, the difficulty predicting and intercepting intergovernmental transfers, and the uncertainty about whether mayors and regional presidents would honor the debt obligations contracted by their predecessors.

This changed in 2008, when SNTA funded technical assistance to facilitate Peruvian sub-national governments' access to financing from commercial banks and capital markets. The goal was to complement existing government transfers and revenues, diversify funding sources, lengthen the maturity of available commercial bank financing, create and strengthen credit histories, and introduce financial discipline. Success included the following results:

- The Metropolitan Municipality of Lima signed a \$70 million commercial bank loan with a local commercial bank in April 2010—the largest market-based borrowing ever concluded by a sub-national government entity in Peru. The loan was backed by a \$32 million IFC partial credit guarantee. Technical assistance was instrumental for the overall engagement with Lima officials and transaction support. In particular, SNTA supported the consolidation of the accounts of the Municipality of Lima and the 19

public companies and other entities it controls; the credit rating from an international credit rating agency; and the development of a five-year macroeconomic corporate report for Lima with projections up to 2015.

- The Regional Government of Arequipa signed a \$10 million loan with a local commercial bank to finance its regional road rehabilitation program. This marks the first time that a regional government in Peru has borrowed without a sovereign guarantee. As with Lima, the loan was backed by an IFC guarantee.

Other Peruvian local governments and public utilities supported by SNTA are also improving their creditworthiness. At least one additional commercial financing is expected to close in 2012.

Lima, driven by its need to achieve higher levels of leverage and by its desire to benchmark its debt management capacity in light of the subnational debt's rapid growth, is reviewing its debt management and planning functions. Corporate-level financing options may be feasible for Lima along the more traditional project-level financing. SNTA support has delivered a rapid market assessment to provide a glimpse of market appetite for long term corporate borrowing by domestic institutional investors, as well as to help inform the views of underwriters, rating agencies, and fiduciary banks. 