From Agenda to Action

Investment in Infrastructure

Report prepared for the Confederation of Nepalese Industries' (CNI) Infrastructure Committee

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Overview

The Nepal Infrastructure Summit 2014, organised by the Infrastructure Committee within the Confederation of Nepalese Industries' (CNI) and its partners, was successful in many ways, including: high attendance, a fantastic keynote speech, excellent speakers and panellists who knew their subject, well facilitated dialogue sessions, a great venue for networking and the presence of young participants. Importantly, participants said that they would sign up and pay for a similar event again. Yet, before the next Summit is held it is important to demonstrate progress on the ideas shared at the 2014 Summit and move from Agenda to Action.

CNI acknowledges that a clear set of actions must be identified, around which a structured discourse can be built that leads to results. This short report responds to this need by identifying critical bottlenecks to investment in infrastructure and recommends critical actions that CNI, along with its partners, can focus on before, and after, the next Summit. Each of the recommendations will help to improve the climate for private investment in infrastructure in Nepal. The recommendations will also help to shape the context, content and structure of the next Summit.

On 25th April 2015 a major earthquake struck Nepal. The initial earthquake, and subsequent after shocks, caused major damage to property and businesses across central Nepal and claimed over 8,700 lives. The impact upon infrastructure was significant, with a total amount identified for recovery in the Post Disaster Needs Assessment of 743 (USD millions), or 18% of total recovery needs, across the 14 most affected districts. This was divided amongst the following types of infrastructure:

- Electricity 186 (USD millions) 25% of total infrastructure recovery needs
- Communications 49 (USD millions) 7% of total infrastructure recovery needs
- Community Infrastructure 45 (USD millions) 6% of total infrastructure recovery needs
- Transport 282 (USD millions) 38% of total infrastructure recovery needs
- Water and Sanitation 181 (USD millions) 24% of total infrastructure recovery needs

Luckily, the critical air and road access points to the Kathmandu Valley were largely unaffected and much of the Valley's urban infrastructure is intact. However, rural infrastructure in the affected districts has been severely damaged.

It is difficult to determine the impact this event has had on investors and investor confidence. It would be naïve to assume that investors would be unaware of the risk of natural disasters in Nepal given that every year many lives are lost through flooding, landslides and avalanches. Having said that, investment appetite is likely to change now that the perception of risk has become a reality. It is possible that some investors may see the disaster as an opportunity to build back better and a chance to invest in the rebuilding of a nation, whilst others may now look elsewhere for safer returns, yet the need for investment in infrastructure will be more important than ever. It is therefore important to provide local and foreign private investors with confidence and ensure that the relief efforts and aid provided by national and foreign governments do not crowd out the space for the private sector to operate and invest in the rebuilding of the nation. Perhaps now, more than ever, there is a need to clearly define the role that the private sector can play in financing and delivering infrastructure projects in Nepal.

With this in mind, an exploratory framework was established to identify the most critical and immediate actions for CNI to take to help increase private sector investment in infrastructure before the next Summit. The report then sets out the critical bottlenecks and actions before providing a brief background on Infrastructure Investment and Development.

Exploratory framework

Speakers and participants at the Nepal Investment Summit 2014 confirmed that Nepal desperately needs to upgrade its infrastructure and institutions that support infrastructure development and investment. They identified a need for:

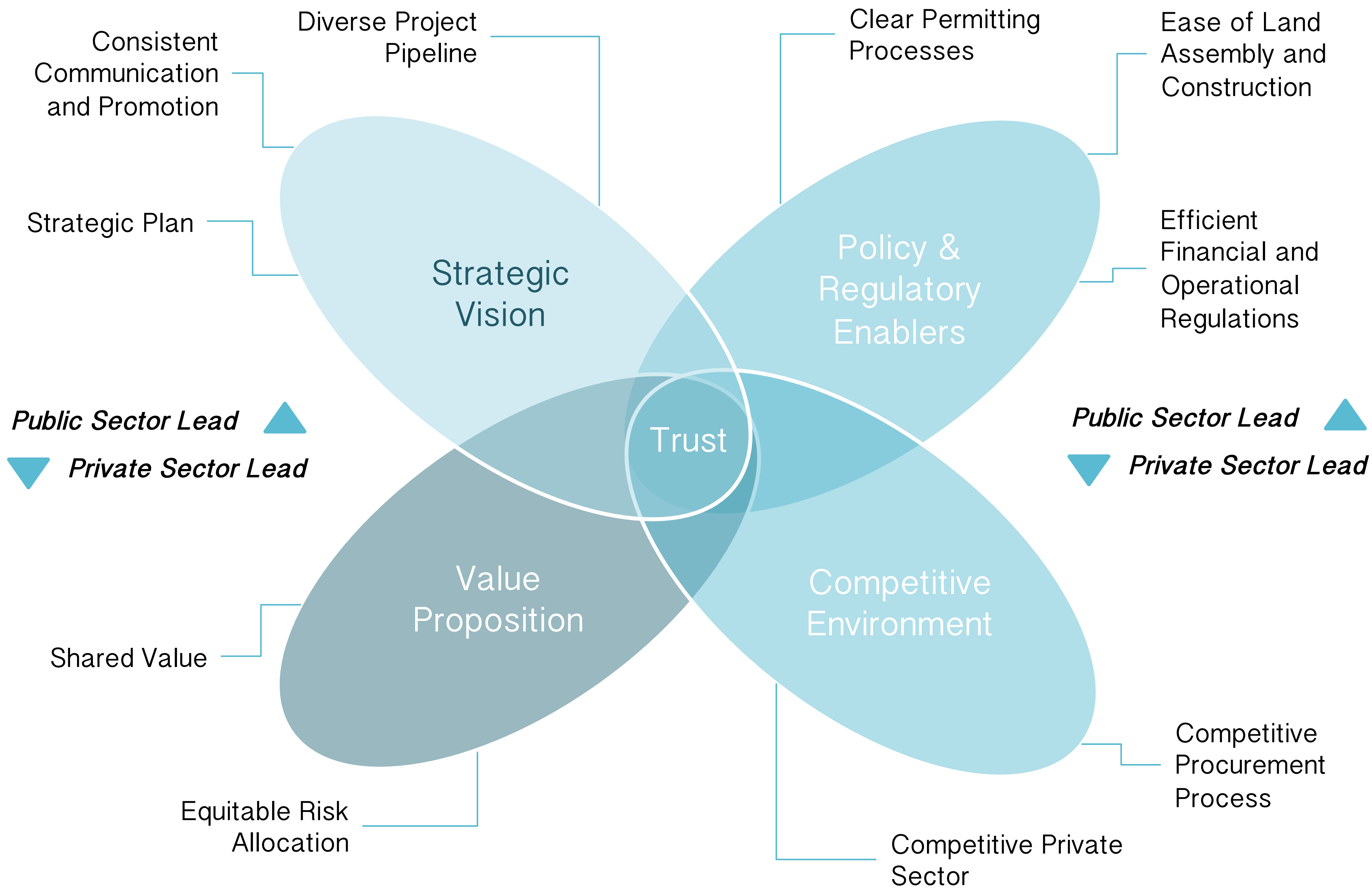
- Stronger mechanisms for the private sector to work with GoN.
- Better mechanisms for allowing private investment and financing of highways, railways, airports, urban infrastructure and transmission lines.
- A more transparent approval process for foreign direct investment.
- Better mechanisms for technology transfer for increasing productivity and efficiency.
- Better implementation of policy and regulations, which is inefficient and often uncertain.
- Streamlining of the bureaucratic decision-making and procurement process, along with better planning, prioritizing and categorizing of infrastructure projects, with more meaningful consultations from the private sector.
- Promotion of healthy competition among private sector players involved in infrastructure development.

Whilst these observations are useful reference points, they do not go far enough or provide specific detail for action. To help assess how the complex variety of interrelated issues combine to restrict private sector investment in infrastructure in Nepal, an exploratory framework was developed by Siddharthinc. The framework is based on the World Economic Forum Infrastructure Investment Policy Blueprint and was adapted to fit the local context following first hand interviews and discussions with leading experts, practitioners and actors in Nepal's infrastructure markets, who either represent leading organisations from the private sector, the public sector, development agencies, consulting firms or are independent. The framework identifies the components of a functioning system that would attract more investment into infrastructure projects in Nepal.

The commentators interviewed as part of this exercise agreed that, above all else, a functioning system should provide investor confidence. Unfortunately, the long length of time it takes to get projects started, delays throughout construction and operational challenges, unclear policies and politics have led to Nepal's poor perception as an investment destination.

At the core of the system there is an acceptance that trust and linkages between the private and public sector should improve, and that progress and action must happen from both sides. In order to do this, the GoN and its respective line ministries have to create a comprehensive vision and plan for the country - identifying major infrastructure projects to realize that vision is critical. The GoN must also do more to speed up disbursement of budgets and ensure alignment of ministries. It should also send positive and welcoming signals out to investors and developers alike.

The private sector must engage with the government to define how it can add value and help to realize that vision. Yet, to make the private sector's value proposition credible, there must be a more competitive environment, where accountability and transparency, and adherence to professional standards and quality are the norm. With commitments for more competition from the private sector, the government can create a policy and regulatory landscape that efficiently achieves the vision and maximises the value proposition offered by the private sector.



Consistent Communication and Promotion
Diverse Project Pipeline
Clear Permitting Processes
Ease of Land Assembly and Construction
Strategic Plan
Strategic Vision
Policy & Regulatory Enablers
Efficient Financial and Operational Regulations
Public Sector Lead
Private Sector Lead
Trust
Public Sector Lead
Private Sector Lead
Value Proposition
Competitive Environment
Shared Value
Competitive Procurement Process
Equitable Risk Allocation
Competitive Private Sector

Strategic Vision

GoN must establish a clear vision for the infrastructure needs of the country beyond the 2022 vision and ensure that plans, strategies and policies prepared by line ministries and departments are aligned.

Strategic Plan and Vision

Perhaps the most critical component of an attractive investment climate is a clear and bold vision set by the GoN of what infrastructure projects are needed, why they are needed, when they are needed, and how they will be delivered. This is required to ensure that a clear role for the private sector is created, that major investments from the private sector are prioritised, and major projects are aligned to deliver maximum benefits for the economy and society. Investors can also be targeted and attracted at critical times to increase efficiency of promotional efforts and permitting processes.

The responsibility for creating a strategic vision and plan for infrastructure projects at a national level has been designated to the National Planning Commission (NPC). The present organization and function of the NPC is based on decisions of the GoN in 1993, while its roles and functions are stated in the Financial Administration Regulations (1999). The NPC creates development plans under the directives of National Development Council (NDC), facilitates the implementation of development policies and programs, provides guidelines and policy targets on forming new budgets to the Ministry of Finance and other line ministries, and also hosts a forum for co-ordination of policy with the private sector through the Policy Dialogue Committee.

The NPC developed a national vision for Nepal in 2014 to graduate from the Least Development Country status by 2022 and set investment targets that are needed in the agricultural, industrial and service sectors to raise Nepali's income, human condition and vulnerability. However, it has become clear from talking to various commentators that despite the efforts of NPC to create an aligned and a consistent approach to national development, especially for infrastructure, one major issue is fragmentation of line ministries and misalignment of strategies and plans.

NPC creates the current three-year interim plans for the country as well as identifying the national priority projects. Yet, so far delivery remains a problem for projects of national significance with most considered to be underperforming and face low rates of budget disbursement. NPC must establish a clear vision and bring ministries together to create a collective plan and strategy to achieve that vision. The development of a coordinated 2030 vision should address such issues.

At a municipal level there is also a need for alignment of vision and communication between ministries and implementing agencies. For example, the Kathmandu Valley Development Association (KVDA), established by the KVDA Act 2012, should lead the coordination of local bodies for development activities in the Kathmandu valley. However, it has been unable to bring together the different agendas set by different ministries and development partners. In an attempt to resolve the need for better urban transport solutions to meet the demands of an ever growing urban population, feasibility studies have been prepared for various transport models, e.g. rapid transit systems and cable cars, but commentators claim little thought is given to which of these projects is most important for the local people and economy. At present, Japan International Cooperation Agency (JICA) is creating an urban master-plan for the city, Asian Development Bank (ADB) is working with the government to improve waste water management, while KVDA has just prepared its 20 year strategy. Clearly, the activities must be aligned to avoid duplication of efforts and resources.

There is a genuine concern that the ad-hoc nature of the planning process allows projects at a national and a local level to be promoted based on individual or political interest. As a basic principle, all major infrastructure projects should be assessed on their contribution to the national and local economy and society and must support national goals and growth. Projects should also be managed with the post-conflict situation in mind to demonstrate peace building, to balance past poverty, and address underlying social discriminations. Clear and consistent criteria for project approval could include, amongst other things:

- Number of jobs created
- Percentage of royalty going into local economy (into schools, health posts, etc.)
- Capacity of project to improve local environmental conditions
- Capacity of project to improve services to locals
- Cost effectiveness
- Resilience to natural disaster (as a community asset and resource at a time of need)

GoN must create a national plan to support its vision, which clearly identifies roles and responsibilities of government bodies, development partners, and the private sector, and identify ways to monitor progress towards the vision. A national planning policy framework should be developed for this effort. CNI could support NPC in developing its 2030 Vision, help identify roles and responsibilities of the private sector, and help monitor progress towards its vision. Physical development plan, energy master-plan, and other infrastructure masterplans need to be developed and aligned with the 2030 vision.

Municipal authorities should also be provided appropriate authority and financial mandate to act and coordinate activities led by departments and development partners.

Diverse project pipeline

There is no clear pipeline of viable and politically acceptable infrastructure projects to attract private investors. Therefore, a diverse pipeline of viable projects must be established and maintained to support the plan and vision set by the GoN. This should include projects in all main types of infrastructure and range in size of investment. The respective roles of government agencies, development partners and the private sector should also be carefully identified in each project. Having a consistent and transparent list of projects will help when promoting Nepal as an investment destination.

A new PPP centre under the secretariat of the NPC, as outlined in the new draft PPP policy, could maintain the pipeline for PPP projects. The centre can set the criteria for projects to be included in the pipeline as well as identify the investment and technical needs required from the private sector for those projects.

Consistent Communication and Promotion

Major infrastructure projects identified and included in the pipeline must be consistently communicated and promoted to domestic and foreign private investors. Most importantly, projects should be prioritized and promoted at critical times to ensure that resources are effectively gathered and deployed. The GoN should be able to identify what private investment it requires and send a strong signal to attract investors. Clear and consistent communication of the purpose and benefits of an infrastructure project can also help to improve community relations and avoid conflict.

Various sources have suggested that the GoN, and respective ministries, including the Investment Board of Nepal (IBN), has failed to consider or treat large investors as VIPs. For investors of any size it is important that they feel wanted and believe that their contribution to the national economy is valued. This is especially true for Non-Resident Nepalis (NRN) and other foreign investors who have the luxury of choosing a country and not simply a project to invest in.

For foreign investors, it is unclear where to look for information and which ministry or department to approach first. For example, the information is held on different websites and is not always consistent or clear: on the DoI and the MoI website, on the Indian Embassy, US Embassy, the IBN website for larger investors, etc. GoN should make information held on all major government websites promoting investment in Nepal consistent. The process must be extremely clear. An investor must know exactly where to start the investment process, which ministry or department to contact first and ideally there should be one central focal point (and central website) throughout the process.

Value Proposition

Private sector must clearly communicate its capabilities and capacities in investing in and developing large infrastructure projects.

Equitable Risk Allocation

There are major risks associated with investing in Greenfield infrastructure projects and it is natural that these are set at an acceptable level to match the respective returns, expectations, and capabilities. The following points should be considered in order to find an appropriate mechanism for balancing risk and creating value.

- In Nepal, if a contractor defaults on an infrastructure project then the lender becomes disproportionately liable and is unsecure.
- Nepali law does not adequately address financial models for limited-recourse financing. Laws such as the Insolvency Act, 2067 and clauses in the BAFIA act relating to liquidation are insufficient to address this issue. Amendments to the Banks and Financial Institutions Act (BAFIA) are needed to allow for limited-recourse financing, especially regarding collateral requirements. For example, signed PPAs can be used in non-recourse financing as security. This issue is especially troubling for international lenders who look for laws on limited recourse financing where lenders have rights to intervene in projects should developers fail.
- Nepali banks are also limited for project financing because of the NRB directive related to Single Obliger Limit and Credit Concentration*.* The directive restricts a bank from concentrating too much of its portfolio on a single project. The clause is meant to maintain stability in the financial sector, but has limited local investment into infrastructure projects.
- There are issues regarding how to secure movable property that could be resolved with a secure transaction law. The Secured Transaction Act of 2006 controls how loans are secured against movable assets. However, its implementation only began in mid 2014, and will need to be strengthened. The implementation is supported by the Credit Information Bureau of Nepal (CIBN) which can act as a secure transaction registry.
- Foreign lenders cannot take immovable assets as collateral without taking approval of the Cabinet. The Loan and Guarantee Act, which covers this issue, is almost 50 years old and needs amendments, or replacement, to include foreign lending provisions.
- Foreign currency risk and trade agreements sought in dollars for greater security and certainty.

Proposed amendments to the BAFIA Act are currently being addressed. Provisions within the amended act will develop non-recourse project financing models. The amendment should also focus on allowing new financial institutions, such as an infrastructure bank, to focus on financing infrastructure undertakings by using long-term institutional deposits, equity and leverage instead of short-term retail deposits. The idea of creating an Infrastructure Development Bank have risen before, even in 2007, with the proposed share structure as 31% for government, 29% for multilateral donors, 20% for

Banking and Financial Institutions (BFIs) and 20% for local business houses. However, it did not progress due to lack of legal provision. This initiative is being revised as per the latest Budget.

Without an acceptable and equitable allocation of risk, Sovereign Guarantees or Multilateral Banking Agreements will be needed to encourage significant foreign investment into Nepal's large infrastructure projects. Development partners can help here. For example, the Work Bank has provided a partial risk guarantee of $100 million for the Upper Trishuli I, and such methods can be replicated to other large scale projects as well.

A new PPP centre, proposed to fall under the NPC, can better facilitate future PPP programs. Each ministry will have a new PPP cell that the PPP centre coordinates with to approve projects. The PPP cells and centre will facilitate the design, development and operation of PPP projects. The new PPP policy draft, seeking to consolidate the Build, Own, Operate and Transfer (BOOT) Act, 2063, will also set up three types of funds to help implement PPP projects. These are the Project Preparation Facility Fund, Viability Gap Fund, and the Revolving Fund for land acquisition. Each of these can help to incentivize private investors and offset risk.

Shared Value

Projects should be designed to create maximum value for government, society and the investor. Yet, there needs to be a clear indication that private investment will seek an appropriate financial return. It should also be made clear among the public that the private sector is accountable to higher standards of efficiency and quality in delivering essential infrastructure projects than the government. Communication from the private sector, therefore, is crucial in explaining their financial gains from the project along with the shared value they are creating for the society and local economy. Good communication from the private sector can lead to better local relations and avoidance of conflict. In particular, the issue of local shares should be addressed through a public dialogue and a national consensus. This will give investors certainty when preparing financial models and appraisals.

The PPP centre and cells in related ministries can become useful tools for promoting shared value. The centre has to filter and promote projects that provide the most societal benefits and that contribute to the GoN's 2030 vision. Carefully designed risk-sharing mechanisms will ensure that projects provide good returns for society, government, and investors.

In many other countries, especially India and China, new financial models have been deployed that offset global carbon emissions. One example, is the Clean Development Mechanism (CDM), which could be introduced to create more shared value in various PPP projects. Nepal, with minimal green house gas emissions, can be compensated through finances and technical expertise by more developed and higher green house gas emitting countries. A working group should be set up to discuss how to increase Clean Development Mechanism (CDM) and voluntary carbon offsets for large infrastructure projects in Nepal with the findings presented at the next Summit.

Competitive Environment

Private and public sector must promote competition and establish competitive practices.

Competitive Procurement Process

The public procurement system in Nepal has to encourage more competition among private sector participants. Public offices as well as private firms lament on the lengthy procurement processes. Not only do these processes erode confidence in Public Enterprises (PE), but also in the contractors and suppliers who sell their goods/services. Improving the procurement process requires effort from both the public and the private sector. Yet, there are initiatives that the private sector can also take to complement the policy changes the government has undertaken.

The government has introduced changes to the Public Procurement Act 2007 (amended). However, commentators still believe there is more room for improvement. A new legal provision, Ordinance 2015, has been included in the Act that allows PEs to fast track procurement decisions, encouraging PEs to become more efficient and competitive. New provisions in the Act seek to remove the incentive for ultra low bidding by requiring contractors to provide additional performance guarantee on top of the existing guarantee, should the bid amount be lower than 85 percent of the project's estimated cost.

These initiatives are positive steps, yet the procurement process needs to be strengthened further. Financial and technical bids must be assessed separately, and the e-bidding process has to be amended to account for differing procurement rules for different donors. The private sector can take a lead in supporting bidding processes by supporting mechanisms to promote competition and quality.

Competitive Private Sector

The private sector must do a better job at building, operating and maintaining infrastructure projects than the public sector. It should be more efficient, innovative and demonstrate that it is capable of delivering complex projects. Firms must be able to signal their capabilities appropriately. Concurrently, the government needs better mechanisms to filter and recognise/reward firms that do higher quality work. Such mechanisms can take the form of higher performance guarantees, delayed payments, or a more transparent platform for bidding. Excuses for poor quality projects should not only fall to the government.

The private sector must improve their professional standards. This relates to understanding and valuing contracts. It also means adopting global standards of accountability and transparency in performance and operations. Companies must also promote good employee rights based on meritocracy, along with good practices of corporate governance. Doing so allows the local private sector to satisfy foreign due diligence requirements for more investment, partnerships, etc.

A spirit of innovation and competition for delivering quality should be sought amongst firms. Technical ability and professionalism should be promoted through awards. CNI should enforce strong standards of corporate governance amongst its members and promote the adoption of international standards of accounting. Members should voluntarily adopt guidelines for participating in infrastructure projects, similar to the OECD *Principles for Private Sector Participation in Infrastructure.*

Policy and Regulatory Enablers

GoN must make policy changes to create a more efficient and attractive investment climate and provide clarity and certainty to investors on key processes in the investment in and development of infrastructure projects.

Clear Permitting Processes

More accountability and clarity is needed regarding the approval processes for investment, setting up a business and any other form of licencing for investments. The issue of threshold remains a concern for the one window policy, as the Investment Board of Nepal (IBN) deals with mega infrastructure projects and Industrial Promotion Board deal with all others. This implies medium size projects may not get the attention they deserve.

There are changes in the short term that can mitigate major limitations of the IBN to facilitate progress of large infrastructure projects:

- IBN needs to be strengthened with full paid staff, including a dedicated legal team, and should not rely on consultants.
- IBN is treated as an outsider by other ministries and needs to graduate from its role of only recommending projects to government bodies.
- Granting of the investment license has to be done by DOI, as IBN does not have the authority to provide a license.
- There is no provision or ability to fast track projects which IBN promotes or recommends for license.
- Project Development Agreement (PDA) is not bankable since it is only a general agreement. An amended PDA must be developed for each specific project and this is where the specific risks and issues really start to arise. IBN has therefore not been very effective in its goal of bringing investment as it has only secured two general PDAs.

The Investment Board Act will have to be amended to give IBN more influence and capacity. Yet, the IBN must also improve its transparency and speed of delivery.

Completing the EIA is often a slow and cumbersome process that is overly bureaucratic and intensive. As a result, private sector developers and investors often see the EIA as a burden, rather than as a tool to futureproof a project/investment. The specific process related challenges include:

- Lack of trained and qualified staff within the line ministries capable of dealing with the large number of EIA submissions
- Approval is required in different departments and line ministries creating a delay to the process as files move from one department to another, where personnel review the same documents.
- Key data sets used to assess project feasibility and design (e.g. water, soil etc) may not be consistent or may be difficult to retrieve from departments.

Poor connectivity and coordination between ministries and access to information and public data are major issues that confuse potential investors on key processes. At worst, some commentators have criticised ministries and secretaries for not considering important projects as their core functions. Human capacity of civil servants is another reason for poor communication between government departments and poor progress of infrastructure projects. Civil servants are frequently moved between departments and not provided with sufficient support and learning; there is a lack of institutional learning capacity. Civil servants are, therefore, unable to adequately deal with a diverse set of project stakeholders, such as developers, investors, promoters, etc.

GoN Ministries e.g. water, geology etc. should be encouraged to review mechanisms for holding and sharing of public data with interested private sector investors.

The government did introduce a provision of signing work performance contracts between secretaries of ministries and project chiefs. However, these provisions were not implemented sufficiently, and ministers and secretaries have not made project chiefs nor contractors any more accountable for delivering projects. The NPC also launched a program to train about 400 civil servants from the Ministry of Energy, Ministry of Finance, Ministry of Industry, Ministry of Commerce and Supplies, and the Ministry of Physical Infrastructure and Transport, especially those that dealt with the private sector, to enhance their capacity in encouraging investments. The program also intended to include private sector employees but it never went ahead.

Ease of Land Assembly and Construction

Project developers, development partners, and government officials claim that land acquisition is a major issue hindering progress in major infrastructure projects. Land assembly needs to be easy for large Greenfield projects. However, local communities are often seen as an obstacle instead of a partner. Developers and government officials claim that locals hike land prices to exorbitant amounts upon discovering that their land is to be part of a lucrative project.

The government is making efforts to resolve disputes arising from land assembly, yet competing claims over land and jurisdiction remains a major hurdle. The Land Acquisition, Rehabilitation, and Resettlement Policy for the Development Projects Policy has recently been endorsed by the cabinet to ease land assembly. The new policy specifies that even if 75% of owners of land to be acquired approve the compensation then it would be considered approved by all affected people. The new policy also specifies that the price of land will be based on the price maintained whenever the government issues a land acquisition notice for a project. A land compensation committee, headed by the chief district officer (CDO), and including affected people, survey office, land revenue office, project chief and expert will determine the price of land to be acquired.

Efficient Financial and Operational Regulations

Nepal has well-drafted and clear laws on tax but the problem remains a lack of compliance. At worst this is seen in cases of proven tax avoidance. For example, forty percent of registered corporate income tax payers in the last fiscal year did not file tax returns, while thirty one percent of firms registered under VAT did not make the filing (according to the Inland Revenue Department). Commentators suggest that the private sector is discouraged from paying taxes because of poor disbursement rate of the central and local government. According to NRB estimates for last year, the government has nearly Rs. 100 billion unspent in the treasury. As a consequence, the private sector may not keep accurate accounts and may exaggerate debt/equity ratios or losses to avoid taxes. If there is more trust and compliance with the local tax laws then it is likely that companies will be more accountable and transparent. The GoN has to introduce better mechanisms for tax collection and revenue disbursement that creates incentives for private sector and civil society to pay taxes and demand services.

Clearer institutional arrangements are also necessary, especially when dealing with foreign investment. The Department of Industry (DOI) was for a long time a one window for all foreign investors. Yet, the DOI has only been able to provide recommendations. Foreign investors are required to visit the Department of Immigration for visa purposes, the Ministry of Environment for conducting Environmental Impact Assessments (EIA), and the Department of Revenue/Customs for obtaining incentives or exemptions. Furthermore, DOI focuses mostly on equity foreign investment, and its consideration of foreign debt as foreign investment is not quite clear. The Investment Board of Nepal does claim to be a one-window facility for large foreign investors, yet larger investors also face issues similar to smaller investors going through DOI.

Stronger and consistent regulation across all major financial classes is also required. The banking and financial institutions are fairly regulated due to the autonomy that NRB maintains as a separate body. However, the Financial Sector Assessment Program (FSAP) of the World Bank and IMF (in 2013) claimed that lack of sufficient skilled staff members and inadequate IT infrastructure hampers the supervisory capacity of the NRB. These inherent weaknesses mean that regulation of BFIs is still compliance based, rather than risk-based. A report of the assessment is not available to the public. Regulation of securities and insurance products, on the other hand, is even weaker because their regulating bodies (SEBON and the Insurance Board) enjoy a lower level of autonomy than the NRB.

Other traditional investment structures widely available in most mature economies and already seen in the local market, such as pension funds and private equity, are not regulated at all, and need to be.

Trust

Underscoring all these initiatives, from both the government and the private sector, is trust. A history of contractors that default, claiming fluctuations in materials pricing, inflation, labour or skill shortage, and poor professional standards, accountability or transparency has led to a poor reputation of the private sector. Similarly, the low rate of government disbursement for infrastructure related projects has led to major hold ups for major projects, especially for roads, creating a similar feeling of inefficiency and lack of urgency.

A respect for the role each party plays in developing infrastructure projects is required along with recognition of quality and competition. All parties must commit to undertake initiatives to increase trust between one another and demonstrate commitments for the long term. The Summit itself will be a useful tool to bring interested groups together and build trust.

Critical bottlenecks and actions

Critical Bottleneck 1 = Finance Risk

1. Support the GoN to implement the following high-level policy reforms.
    - Amend the Insolvency Act, 2067 and the Banks and Financial Institutions Act (BAFIA) to allow for limited-recourse financing.
    - Amend NRB directive related to Single Obliger Limit and Credit Concentration to reduce limit on banks lending portfolio.
    - The Debt and Guarantee Act, should be amended, or replaced, to include foreign lending provisions.
    - Revisit the creation of an Infrastructure Development Bank.

Critical Bottleneck 2 = Land Assembly and Community Engagement

2. Encourage project developers and investors to carefully consider all "affected people" and ensure that demographic and socio-economic data is properly collected and analysed during the preparatory phase and any compensation package is incorporated into the feasibility study.
3. Help GoN and local private sector to work together to develop communication strategies for major projects. Clear protocols and consistent messaging should be established for informing local communities of the purpose, impact and benefits of large-scale projects to reduce the risk of conflict.

Critical Bottleneck 3 = Environmental Impact Assessment (EIA) Process

4. Support the GoN to implement reforms of the EIA.
    - Lobby government to increase capacity of the EIA team and to establish a single EIA Committee to review across all relevant ministries and allow single approval.
    - Encourage government to create open and public data sets for areas (e.g. watershed).
    - Run an awareness raising campaign amongst the private sector to promote the importance of the EIA for futureproofing a project/investment.

Critical Bottleneck 4 = Public-Private Partnerships

5. Work with NPC to ensure the effective delivery of the PPP Cell, the project pipeline and associated funds (Project Preparation Facility Fund, Viability Gap Fund and the Revolving Fund).

Critical Bottleneck 5 = Lack of Competitiveness and Trust

6. Work with GoN to clearly set out the role of the private sector in key infrastructure projects in the reconstruction, and to achieve LDC Graduation (2022) and Middle Income status (2030).
    - Support NPC to train 400 civil servants on "private sector interaction".
7. Help the private sector to voluntarily raise performance standards and move to a position of self regulation and competition/ pride related to timeliness, quality, labour relations and sourcing of materials, among other things.
    - Establish awards for excellence.
    - Create a register of quality and delivery and work with GoN to recognise excellence in procurement process.
    - Promote strong standards of corporate governance, accountability and transparency.
    - Promote adoption of the OECD Principles for Private Sector Participation in Infrastructure.

Background on Infrastructure Investment and Development in Nepal

Nepal suffers from systemic problems in infrastructure development and investment. Poor existing infrastructure, along with political instability, together, are the two biggest challenges to Nepal's investment climate and growth (Afram & Pero, 2012).[1]

Provisions in the Public Procurement Act, the Land Acquisition Act, poor preparation before project implementation, and disruptions in the supply of construction materials are other bottlenecks to rapid infrastructure development.[2] Donors also raise issues of frequent staff transfers, the long public procurement process and land acquisition and forest clearance obstruction in the projects they fund. However, many commentators suggest that it is not simply government policy that needs to be clear. Rather, what is needed is more consistent application or implementation of the policy or regulation.

Low capital expenditure of ministries responsible for infrastructure development also highlights the need to carefully address private sector participation in developing connective infrastructure. The Chief Secretary himself claims that low capital expenditure from government agencies is primarily because of mismatched policy between agencies, excessive procedures, and coordination flaws among various government bodies and contracting partners.[3] Such misalignment and unclear implementation of policies and regulations creates even greater uncertainty for investors and increases the project risk in the early stages of development. These issues remain and have become more relevant now as Nepal looks to rebuild itself after the earthquake.

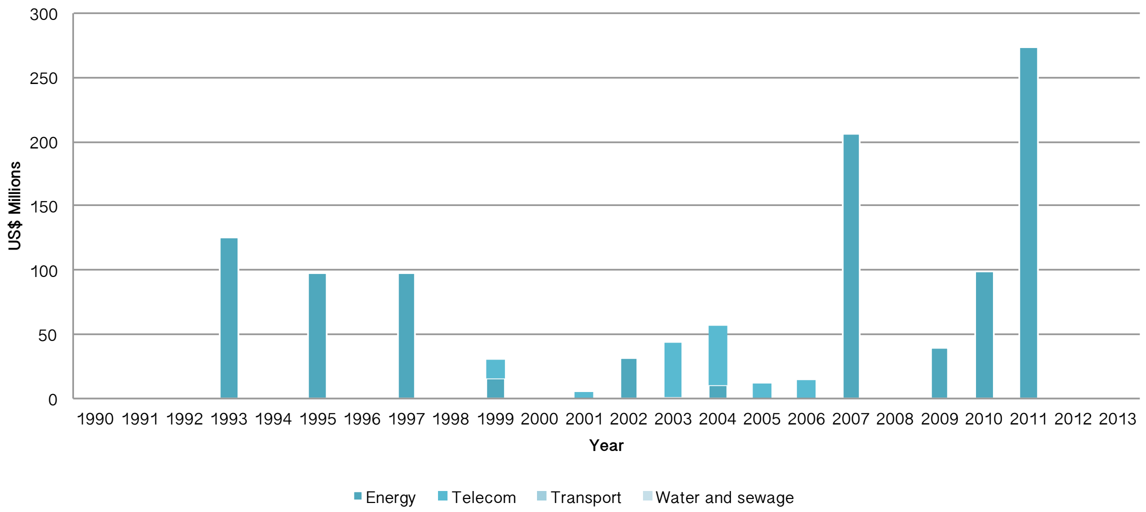
Pre-earthquake estimates identified that for Nepal to undergo rapid growth and achieve its vision of becoming a developing country by 2022, an investment of 8-12 per cent of its GDP (in 2010 terms) is needed annually on infrastructure (World Bank, 2014).[4] It is likely that the impact of the earthquake will revise this estimate upwards, but a formal assessment is needed. A greater involvement of the private sector is, therefore, required in financing, building and operating infrastructure to make Nepal more competitive and to meet its development goals. Yet, private sector commitments to infrastructure from 2007-2012 stood only at 0.66% of GDP (Luis Andres et al., 2013[5]).

Private participation is needed in building new infrastructure for electricity, transport, water and sanitation, irrigation, telecommunication, solid waste systems etc., and also in strengthening and rehabilitating existing assets. More private sector participation will also create a necessary alternative to the inertia that comes with mobilising government resources.

The Government of Nepal (GoN) has begun partnerships with the private sector on electricity and telecommunications, especially in terms of financing. The World Bank's Private Participation in Infrastructure Database confirms that most infrastructure projects in Nepal where the private sector has been involved have been in either energy or telecoms.

[1] http://books.google.com.np/books/about/Nepal_s_Investment_Climate.html?id=sQp5Gp5tMSMC
[2] http://www.ekantipur.com/2015/03/20/business/4-key-ministries-show-low-capital-spending/403043.html
[3] http://www.ekantipur.com/2015/03/20/business/4-key-ministries-show-low-capital-spending/403043.html
[4] WB (2014) A vision for Nepal Investment Infrastructure Inclusion
[5] Andrés, L., Biller, D., & Herrera Dappe, M. (2013). Reducing Poverty by Closing South Asia's Infrastructure Gap.

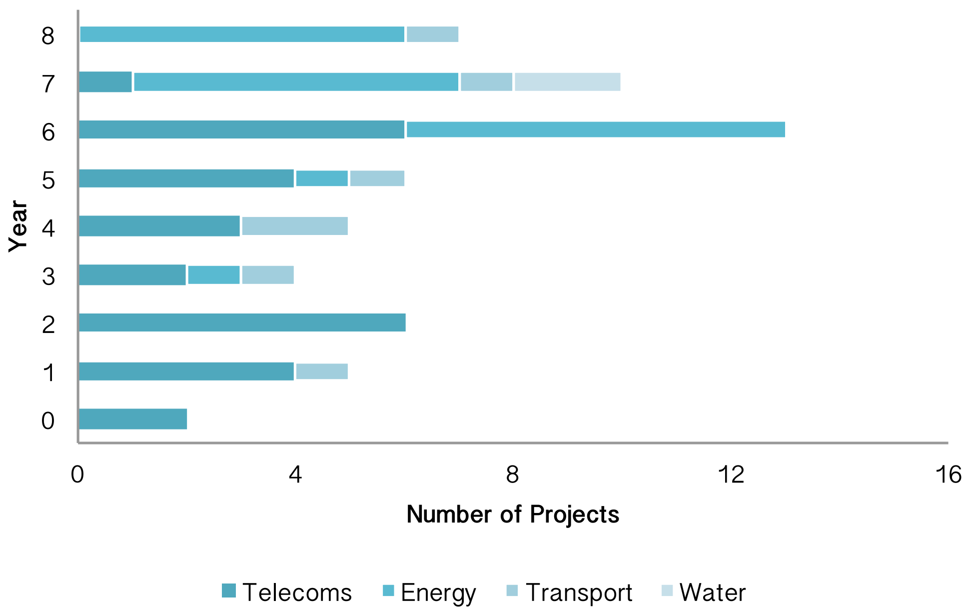
Figure 1: Investment in projects by primary sector



Source: World Bank Private Participation in Infrastructure Database for Nepal

This trend can be observed in other post-conflict countries too. Schwartz & Halkyarg (2006) find that telecommunication seems most attractive for private investors in countries immediately following conflict. This is followed by electricity generation and distribution, which typically emerges three years after the end of conflict and increases in frequency after five years (Figure 2). Transport sectors, which often open up to private sector participation several years after conflict, are less attractive since they are vulnerable to political risk. Water and sanitation receive the least investment and are the last to receive involvement from the private sector (Ahman LSE, 2014).

Figure 2: Sector distribution of infrastructure projects with private participation by year after conflict



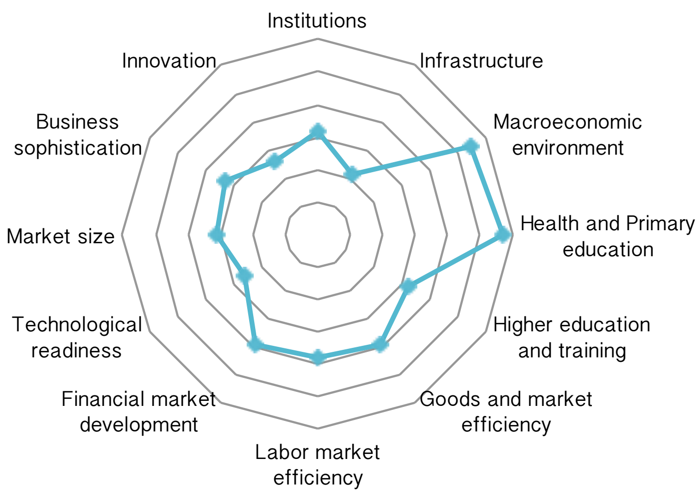
Source: World Bank (2004) The Private Sectors Role in the Provision of Infrastructure in Post Conflict Countries

Note: Based on data for 10 countries that have emerged from war since 1990 and for which eight years of consistent data were available: Azerbaijan, Cambodia, El Salvador, Georgia, Lebanon, Mozambique, Nicaragua, Rwanda, Tajikistan, and the Republic of Yemen.

The pace of private involvement in infrastructure development across Nepal in sectors other than hydropower and telecoms, e.g. roads, airports, transmission lines, water and waste systems, has been slow. Moreover, because of an inadequate emphasis on connecting infrastructure such as transmission lines and access roads, delays in hydropower development have arisen, which continues to frustrate developers and investors.

At present, Nepal ranks poorly as a global investment destination and remains unattractive for investors. According to the World Bank Doing Business in Nepal report, Nepal's rankings have not improved for any processes other than for obtaining construction permits and registering property. Rankings in other areas, such as starting a business, getting electricity, getting credit, paying taxes, trading internationally, resolving insolvency and protecting minority investors have worsened since 2014.[6] Nepal's debt is not even rated by credit rating agencies such as Moody's, Fitch, or Standard & Poor's, making it difficult for international investors to understand risk in Nepal. To fill this ratings gap the World Bank's Poverty Reduction and Economic Management unit came up with a shadow sovereign rating for Nepal. As of 2012, Nepal's shadow rating is CCC+, indicating Nepal as a "High Default Risk" country for investment.[7] To compound this negative image, Nepal's Global Competitiveness Index has been stagnating as well.[8] Over the past three years, the country's infrastructure has not improved, and neither have public and private institutions.

Figure 3: Competitiveness Index Sub-pillar ratings for Nepal in 2015



Source: World Economic Forum Global Competitiveness Report, Nepal

Note on Methodology

Special attention was given to four types of infrastructure: roads, transmission lines, airports and urban infrastructure, because of the relevance to the private sector and the availability of suitable projects in Nepal. However, the recommendations are equally relevant for other complex infrastructure projects that require large amounts of finance, land assembly, community engagement and liaison with various government departments.

Analysis of each of the four types of infrastructure, as well as further information on policy and other related issues, is captured in a separate Appendix.

[6] http://www.doingbusiness.org/data/exploreeconomies/nepal/#dealing-with-construction-permits
[7] http://www.ekantipur.com/the-kathmandu-post/2012/01/29/related_articles/a-shadow-rating-of-ccc/230999.html
[8] http://reports.weforum.org/global-competitiveness-report-2014-2015/economies/#economy=NPL