

## ASSESSMENT OF ADB'S PRIVATE SECTOR ACTIVITIES

**A. PRIVATE SECTOR DEVELOPMENT, POVERTY REDUCTION, AND GOVERNANCE**

ADB views PSD as an effective means to achieve its overarching objective of poverty reduction. Sustainable economic growth, based on increased productivity, is the key to winning the war against poverty. The private sector will be the engine for economic growth, creating jobs and increasing incomes necessary to lift people out of poverty. Recent studies have revealed strong empirical evidence of the links between growth and private investment, job creation in the private sector, and poverty reduction (IFC 2000c).

A study on the relationship between job creation and poverty reduction in 80 countries from 1987 to 1998 concluded that private firms created 4–80 times as many jobs as public sector firms, depending on the country (Table 23). One survey tracking specific poor individuals over time shows that finding a job (or a family member finding a job) is a major path out of poverty (Pfeffermann 2001). Most people escaping poverty find jobs in private firms, not in the public sector. In this sense, PSD has a sustainable effect on poverty reduction.

**Table 23: Private Firms as a Source of Job Creation**  
(selected developing countries)

Country	Period	Job Creation ('000)		Job Creation Ratio Private to Public
		Private	Public	
PRC	1996-2001	27,139.0	0	87:1
Mexico	1989-1998	12,431.0	143.0	16:1
Turkey	1987-1992	1,490.0	91.0	13:1
Kenya	1993-1998	173.0	13.0	10:1
Bolivia	1994-1997	181.0	18.0	3.6:1
Gabon	1992-1996	4.7	1.3	

Sources: *China Statistical Yearbook*. 2002. Pfeffermann, 2000. Private Sector Development Strategy – Directions for the World Bank Group. 2002.

The PRC's experience is more complex due to its size and nature of the country. However, the above hypothesis is applicable. PSD has had a significant impact on poverty reduction. A recent unpublished ADB study shows that provinces and cities that have a high share of private sector activity usually have a much lower level of poverty (ADB 2001a). The relationship between per capita GDP and the share of private sector employment to total employment in 30 provinces clearly indicates a relationship between the contribution of private sector employment to the level of income. On average among provinces, for every 1% increase in the share of private employment, there is a corresponding increase of CNY164 (\$20) in per capita GDP.

Good governance is also essential for PSD and poverty reduction. Good governance establishes the rules of the game for the private sector in a clear and transparent manner. Good governance improves transparency, predictability, accountability, and participation. These dimensions are all needed for the private sector to be able to make sound business decisions, reduce risk, and operate efficiently. The poor are most vulnerable to public sector inefficiencies, corruption, and waste (ADB 2002c).

## B. ADB'S SUPPORT TO PRIVATE SECTOR DEVELOPMENT

ADB has provided assistance to promote PSD in the PRC within a framework that has three strategic thrusts (i) to help establish an enabling environment for the private sector; (ii) to generate business opportunities in which the private sector can participate; and (iii) to catalyze private investments by mobilizing additional resources through direct financing, credit enhancements, and risk mitigation instruments. The first 2 have been pursued through ADB's public sector window, mainly with TA operations and loans to help address infrastructure constraints. The third has been operationalized through investments in, and loans to, private individual companies by ADB.

### I. TA Operations

As of 31 October 2002, ADB has provided 46 TAs totaling \$25.6 million in support of PSD in the PRC.<sup>92</sup> Support can be broadly classified into four categories: (i) financial sector support (15 TAs—\$6.64 million); (ii) an enabling environment for private participation in infrastructure (16 TAs—\$10.20 million); (iii) laws to promote PSD (3 TAs—2.25 million); and (iv) enterprise support including TAs to assist SMEs (12 TAs—\$6.47 million).

ADB's TA operations reflect three trends in response to emerging needs in the private sector: (i) a shift from a broader industry study in the financial sector to more focused enterprises support such as capacity building; (ii) focused topics to address specific constraints on participation by the private sector in infrastructure, such as water tariffs studies; and (iii) studies in response to emerging challenges of supporting the rule of law (Appendix 13).

#### a. Financial Sector

Over the past 14 years, ADB has provided TA in the financial sector to help develop the emerging nonstate sector. In the early 1990s, TA projects centered on broad industry studies such as leasing, VC, and securities market development, to identify policy and legal constraints. In the late 1990s, the focus shifted to capacity building of particular financial institutions and regulatory organizations (e.g., capacity building of the financial markets' regulatory systems, institutional strengthening of Cinda). Additional TA studies that address the need for enterprise reform are discussed below.

<sup>92</sup> The figure does not include the *Technical Assistance to the PRC for the Jiangsu Highway BOT Project*, which was suspended to change the scope and concept of the project. Negotiations with the Government are under way.

## b. Enterprise Support

ADB's TA for enterprise reform in the early 1990s encompassed a wide range of topics: (i) restructuring of SOEs; (ii) study on social welfare and labor adjustments for enterprises; (iii) TVE development; (iv) enterprise accounting system reform; and (v) a study of the local consulting industry. In the late 1990s, the focus shifted to development of SMEs and PSD.

Currently, ADB is helping the Government develop a policy and regulatory framework to promote SME development and address the lack of access to financing. At the national level, ADB has worked with SETC to (i) provide advice on suitable SME financing policies and mechanisms; (ii) survey and review existing SME credit guarantee fund operations to help prepare a strengthened policy framework for SME schemes; (iii) identify suitable strategies and conditions to facilitate the provision of capital for SMEs from nongovernment sources, including VC funds, specialized commercial SME investment funds, and domestic capital markets; and (iv) design a financially viable pilot equity support scheme and assist in its establishment. This includes advice on creating a supportive legal, regulatory, policy, and institutional environment for their operation. This TA helped prepare the SME Promotion Law that was adopted by the NPC on 8 June 2002. A subsequent TA was provided to help design the SME Development Fund, as provided in the SME Promotion Law (ADB 2002g).

ADB's work in helping to develop SMEs in Shanghai includes (ADB 2000b) (i) advising on best practices for SME credit and credit guarantee scheme (CGS); (ii) developing policies, procedures, and systems for the Shanghai branch of the China Economic Technological Investment Guarantee Corporation (CETIGC); (iii) advising on the supervision of local guarantee funds; (iv) providing assistance to three selected banks (Bank of Shanghai, local branches of Minsheng Bank, and ICBC) in the development and implementation of SME credit risk assessment and management systems; (v) supporting a training program for CETIGC and local bank staff in SME lending; (vi) undertaking a needs assessment for complementary business support services; and (vii) identifying information and data required to assess SME creditworthiness and developing a strategy for collecting, analyzing, and disseminating such information to interested parties in a cost efficient manner.

ADB worked with ACFIC (ADB 2000a) to identify and promote appropriate policies and conditions for private enterprise development and strengthen ACFIC's business support services. ADB supported an enterprise-level study to assess the status of PSD, identify impediments to future development, and assess the need for finance and business support services. A strategy for developing ACFIC's business support and information services at central and local levels was prepared and basic business courses were developed for private entrepreneurs (Box 4). Domestic and overseas training programs were also provided to ACFIC staff and selected local chambers of commerce that provide business advisory services.

## c. Creating an Enabling Environment for Private Participation in Infrastructure

ADB has provided assistance to facilitate PPI. In recent years the TAs took a more focused and targeted approach, directly addressing issues and constraints to such participation. Examples include corporatization in the road sector and water tariffs studies.

**Power Sector.** ADB TA operations in support of private participation in the power sector cover seven TAs totaling \$3.8 million during 1993–2002. ADB's strategic agenda for policy reform in the power sector includes (i) pricing and tariff reforms; (ii) sector restructuring and enterprise reform; (iii) increasing private sector participation; and (iv) promoting the corporatization and commercialization of power utilities and the development of competitive markets in electricity. These ADB-supported reforms will help create an enabling environment for the private sector in the power sector.

**Road Sector.** ADB provided five TAs in the transport sector in support of the private sector totaling \$4.175 million. Since 1995, ADB has provided TAs aimed at creating a market-enabling environment in this sector. Each of these studies identified policy deficiencies and suggested corrective measures. The measures recommended include

- (i) adoption of new legislation assuring the legality of the transfer of rights to assets or asset usage and enforceability of these rights;
- (ii) clarification and revision of regulations and administrative procedures;
- (iii) improvement of levels of transparency and accountability in decisionmaking;
- (iv) expansion of the scope of corporations;
- (v) inclusion of more shareholders in joint stock companies by capitalizing the value of land and resettlement costs and offering shares to municipalities, through which the road passes, banks (in exchange for debt), and heavy users of the road such as mines, refineries, or shipping companies;
- (vi) revision of the approval process (which currently precludes broader international bidding, delays land use certificates, etc.) to encourage competitive leasing or concessioning; and
- (vii) identification of the need to address insufficient traffic level volumes to support investment.

**Wastewater and Water Supply Sector.**<sup>93</sup> Four TAs in the water sector are relevant to PSD. Among them, the two water tariff study TAs implemented over a 4-year period were particularly important to help create an enabling market-oriented environment for private sector participation, thus contributing significantly to water tariff reforms in the PRC.

In line with market reforms, WSCs are being encouraged to recover their operation and maintenance costs and some depreciation. Having appropriate mechanisms for tariff setting will be critical in attracting private investment. ADB provided a TA (ADB 1997b) to study water tariffs and develop appropriate tariff mechanisms to ensure full cost recovery. A major output of this TA was the preparation of the National Guidelines on Water Tariffs (NGWT), which were subsequently promulgated by SDPC and the Ministry of Construction in September 1998. Major features in the NGWT that reflect specific recommendations of the TA include (i) selecting a tariff structure based on local conditions and priorities; (ii) considering a two-part tariff with a volumetric charge and fixed demand charge; (iii) adopting full cost recovery as the main objective in setting and approving tariff levels; (iv) using the public hearings mechanism to disseminate tariff increase plans to the public and obtain their feedback; and (v) adopting a simplified process for tariff regulation by requiring evaluation and approval at the local municipal government level, supported by review and monitoring at the provincial and national levels. The NGWT is expected to improve the long-term financial viability of WSCs and provide for operations and maintenance, and service expansion, which in turn should help increase private sector participation in this sector.

A second water tariff study (ADB 1999b) focused on providing assistance to the Government in developing institutional and methodological capacities to implement the NGWT. The TA assisted in preparing the draft local implementing regulations of the NGWT for Zhangjiakou, Fuzhou, and Chengdu, which were accepted by the relevant local governments. Enactment of local tariff regulations provides a legal basis for regulating water tariffs and ensures transparency and efficiency. The Zhangjiakou Implementation Regulations (ZIRs) were approved by the Zhangjiakou Municipal Government in September 2000. The ZIRs were the first local water tariff regulation under the NGWT. The Chengdu Implementation Regulations was expected to be issued in 2002.

<sup>93</sup> Since 1989, ADB has supported 55 TA studies for approximately \$28 million to address issues relating to water resource management, environment, and water supply.

Public hearings are a mandatory requirement of the NGWT. The TA advocates the use of hearings to obtain the views of the public on water supply and promote public understanding of WSCs, policies, and efforts to develop improved water supply services. Based on the first public hearing, Zhangjiakou increased its water tariffs by 75%.

The NGWT also promotes social programs targeted at the urban poor to mitigate the impact of tariff adjustments. The ZIRs include cash rebates for poor families, laid-off workers, and social aid families under the administration of the Labor Union and Civil Affairs Bureau. The NGWT also requires the tariff structure to include lifeline tariffs for the poor. The TA recommendations, including the achievements in Zhangjiakou, have been acknowledged by the State Council as a good example for tariff reforms. SDPC issued a notice to local governments nationwide recognizing the Zhangjiakou water tariff reforms as a good example for undertaking tariff reforms required by the NGWT. Upon completion of the study, SDPC, the Ministry of Construction, MOF, and other relevant government bodies officially issued a notice on further strengthening of urban water tariff reforms on 1 April 2002, followed by a nationwide videoconference to discuss the Zhangjiakou experience on water tariff reforms on 9 April. Subsequently, SDPC and the Ministry of Construction issued another notice on the national auditing of water tariffs and conducted a related training seminar in April 2002.

Specific impacts of the overall package of reforms are best illustrated by the benefits in Zhangjiakou. The benefits include (i) establishment of the Price Bureau's lead role in tariff administration; (ii) a streamlined water supply administration of the Public Utility Bureau; (iii) a financial plan which is in place for the Zhangjiakou WSC to service the debt within a reasonable time frame while recovering other costs and earning profits; (iv) funds for the municipal government of Zhangjiakou to repay international and domestic loans within 6 years and for future development; (v) funds for the Construction Commission, which is responsible for Zhangjiakou's new water treatment plant, to finish its work; (vi) proposed tariffs that are affordable for domestic customers and a new program for poor households to provide relief from their water bills; (vii) transparency of the tariff approval process through public hearings that will encourage cost control and service improvements, promote understanding of the importance of tariff increases, and support tariff adjustments; (viii) strengthened institutional capacity to control costs and tariff increases; and (ix) improved water conservation by imposition of tariff increases and an appropriate tariff structure. Multiyear tariff adjustment proposals such as the one developed for Zhangjiakou will result in other benefits. First, the underlying financial plan for the proposal provides the basis of a service contract between the municipality and the WSC, which can serve as a tool to control costs. Second, long-term financial planning provides a framework within which to attract private investors.

In the water sector, ADB is focusing on (i) improving the efficiency of water supply and distribution systems through investment in physical infrastructure; (ii) promoting improved corporate governance and commercial management to enhance the potential for future private sector involvement; (iii) improving cost recovery by strengthening tariff systems and structures for raw water and treated water; and (iv) ensuring water resources conservation and environmental protection through the continuing support of legislative and regulatory provisions governing water pollution and natural resources management. ADB water policy encourages the funding of new water supply projects directly through water tariff increases (e.g., Harbin).

#### d. Better Laws to Support Private Sector Development

Helping the Government formulate laws to support PSD is an important feature of ADB's TA operations. ADB has provided \$2.25 million for three TAs that will help formulate key laws and regulations that are necessary for the efficient functioning of a market economy. The TA for the Development of Economic Laws approved in 1999 for \$1.4 million has provided assistance to the Legislative Affairs Commission, Standing Committee of the NPC and Office of Legislative Affairs of the State Council in drafting work for the following new laws or amending existing laws:

(i) Company Law, (ii) Bankruptcy Law, (iii) Trust Law, (iv) Social Security Law, (v) Administrative Licensing Law, (vi) Law on Registration of Enterprises, and (vii) Regulation of Legal Aid. ADB also provided assistance for drafting the government procurement law, the securities law, land administration law, and clean production law.

In 2001, ADB provided assistance to help identify changes to laws and regulations required for the PRC's WTO membership. Required changes include codifying existing administrative practices into written laws and regulations to increase predictability and transparency. This demanding task includes around 200 laws and regulations that need to be reviewed, revised, repealed, and/or incorporated into new laws or regulations. The adoption of the WTO's rules-based system will have widespread benefits for the private sector. The objectives of ADB's assistance in this area are to (i) help the Government make its foreign trade laws and regulations compatible with WTO principles, rules, and obligations; (ii) help the Government determine the institutional setup for regulating foreign trade and investment; and (iii) support the Government's efforts to increase transparency by making legal information public and clarifying laws and regulations on foreign trade and investment.

As the PRC's private sector has emerged, ADB's TA operations in support of PSD have also evolved over time to focus on specific issues and constraints on development. Given ADB's resource constraints and the size of the country, ADB needs to intensify its efforts to identify proper TA topics and issues to respond to the critical needs of the private sector.

## 2. Lending Activities

Through its public sector lending program, ADB has helped create an enabling environment for the private sector by addressing infrastructure constraints. Public sector loans have been provided to finance construction of highways and roads, power plants and transmission lines, and water treatment facilities.

## 3. Private Sector Operations

To catalyze investment in the private sector, ADB employs various instruments such as loans without government guarantees, equity investments, commercial cofinancing, and credit enhancement mechanisms. Administration of existing portfolio projects is also an important aspect of private sector operations.

Other objectives of ADB's private sector operations in the PRC's capital markets include support of PRC efforts to raise corporate governance standards, catalyze transfer of capital and knowledge in capital market institutions, and support PRC efforts in raising the efficiency and competitiveness of capital market institutions in anticipation of WTO reforms. ADB is seeking high quality and creditworthy opportunities in the banking sector, other savings institutions such as mutual funds and pension funds, and capital market institutions such as credit rating agencies, and resolution of the NPL problem.

ADB made its first equity investment in the PRC in 1991, taking a 10% equity in the Xiamen International Bank, the PRC's first Sino-foreign JV bank based in Fujian Province. ADB's involvement catalyzed subscriptions from other foreign investors. As of October 2002, ADB had approved \$151.5 million in loans and \$79.3 million in equity investments in private sector projects. ADB had a portfolio of nine private sector projects consisting of 5 equity investments of \$79.3 million and 4 loans of \$151.5 million, respectively (Table 24). These projects can be organized into two categories: (i) \$126.5 million for three infrastructure projects, and (ii) \$104.3 million for financial sector operations. All these investments confirmed the important role of ADB in mitigating perceived risks and encouraging capital flows. With a funding commitment of more than \$230 million, ADB was able to facilitate investments in development projects worth over \$2.14 billion. On average every dollar of ADB's participation catalyzes \$7 of total investment.

Table 24: ADB Private Sector Loan and Equity Investments in the PRC

Project Name (Year Approved)	Amount Approved (\$ million)			Estimated Project Cost/ Fund Size	Leverage Ratio (times)
	Loan	Equity	Total		
Xiamen International Bank (1991)	–	10.3	10.3		
China Assets Holdings (1991)	–	4.0	4.0	74.1	18.5
Guangzhou Pearl River Power Company (1992)	50.0	–	50.0	352.4	7.0
China Everbright Bank (1996)	–	20.0	20.0		
Fujian Pacific Electric Co., Ltd. (1998) (Meizhouwan Power Project)	40.0	10.0	50.0	740.0	14.8
Chengdu Generale des Eaux-Marubeni (GEM) Waterworks (1999) (Chengdu Water Supply Project)	26.5	–	26.5	106.5	40.2
Liberty New World China Enterprises (2000)	–	25.0	25.0	150.0	5.0
Water Infrastructure Development Facility	35.0	–	35.0	150.0	4.3
China Environment Fund 2002 Limited Partnership	–	10.0	10.0	40.0	4.0
<b>Total Approvals (as of October 2002)</b>	<b>151.5</b>	<b>79.3</b>	<b>230.8</b>	<b>1,613</b>	<b>7.0</b>

Below are notable catalytic achievements of ADB's private sector operations in the PRC:

- (i) *Xiamen International Bank* was the PRC's first Sino-foreign JV bank;
- (ii) *Guangzhou Pearl River Power Company* is one of the PRC's first JV independent power producers that has been operating profitably;
- (iii) *China Everbright Bank* is the first domestic bank that was allowed to have foreign equity participation;
- (iv) *Fujian Pacific Electric Company* is the first 100% foreign owned independent power producer in the PRC that was approved by the State Council. Because of ADB's involvement, this deal was closed during the height of the Asian financial crisis. This project received two prestigious "deals of the year" awards from international trade magazines; and
- (v) *Chengdu Generale des Eaux-Marubeni Waterworks*: ADB played an essential role in structuring transparent international bidding for the PRC's first BOT water supply project. This project received four international awards for excellence (Box 10).

A recent private sector project in the PRC was a \$25 million investment made in 2000 in a \$150 million equity fund aimed at SMEs. ADB's partners in the fund, the New World Development Company Limited of Hong Kong, China, and the Liberty Mutual Insurance Company of the US, are well known for their investment expertise and networks. This fund is designed to identify high growth SMEs and help increase their competitiveness by initiating the best corporate governance and management practices. The fund is focusing on four core business sectors: health care, consumer products, building materials, and automotive midstream and downstream services.

The fund plays an active role throughout the investment process by identifying prospective investments, actively managing and building products, and ensuring business efficiency and profitability at all levels. Due diligence and a critical examination of operational strategies and financial soundness are conducted to identify potential investee enterprises, and appropriate international strategic partners are selected to make contributions in technology, market expansion, management skills, and capital. To ensure that each project achieves excellent results, the fund's investees are provided with management support by a team of more than 40 marketing, financial, and management professionals in Hong Kong, China and the PRC. This team also monitors the entire process of the Fund's investment management. In addition to investment screening and negotiating

contracts, the team maintains board representation and ensures implementation of financial control over each project. Upon proven success, the fund replicates and extends the project platform across the country. ADB's main objectives in supporting this fund include (i) strengthening private sector enterprises by adopting best practices and corporate governance; and (ii) strengthening foreign investors' confidence in investing in the PRC's private sector.

As of 31 December 2002, the fund invested in eight companies in industrial sectors such as electronic/mechanical components, ceramic glass, pharmaceutical, food and beverage, automobile dealership and services, and security products/systems/services.

The PRC is also among the countries targeted by three regional investment funds supported by ADB investments (Table 25). ADB has invested \$75 million in these regional funds that support primarily private sector investments in infrastructure projects.

**Table 25: Regional Funds Investment/Loans in the PRC**  
(\$ million)

Name of Fund	ADB Investment	Fund Size
Asian Infrastructure Fund	20.0	780
Asian Infrastructure Development Co. Ltd.	30.0	400
Asian Infrastructure Mezzanine Capital Fund	25.0	245

As of 31 December 2001, Asian Infrastructure Fund invested in four companies: (i) a toll road operator for its investments in five provinces; (ii) a port operator; (iii) a power venture; and (iv) a paging operator. Asian Infrastructure Development Company invested in two companies in the road and telecommunications sectors. Asian Infrastructure Mezzanine Capital Fund invested in one company in the telecommunications/internet sector.

Recently, ADB approved a new \$10 million investment in the China Environment Fund, which aims to raise \$40 million of equity capital. The China Environment Fund is the first private sector fund in the PRC dedicated to addressing environmental issues. The PRC faces mounting environmental challenges and, based on the huge costs involved, cannot afford to clean up the environment without private sector assistance. The fund has made an investment in industrial and hazardous waste treatment companies in Shenzhen.<sup>94</sup> ADB also approved a \$35 million loan in a \$150 million water infrastructure development facility.

**Lessons Learned.** ADB's experience in these projects, specifically in infrastructure projects, confirms the need for closer ADB involvement at early stages of project development to ensure a bankable contract structure. Clear provisions on setting and adjusting tariffs for offtake agreements would mitigate investor and lender risk. Projects will need to be scrutinized to ensure that returns are dependent on optimization of operations based on the Central Government's recent guidance that discouraged government entities from entering into fixed return deals (Box 11 and Box 12).

<sup>94</sup> Protecting the environment and promoting sustainable development is one of the main objectives of ADB in the PRC. ADB has provided substantial assistance in addressing the PRC's environmental conditions. By end-2001, ADB had provided more than \$2.4 billion in loans and 93 TA grants totaling more than \$71 million for environmental improvements in the PRC.

Box 11:

### Lessons Learned from Private Sector Investment in the PRC

**Fair Deal.** “At times, negotiating a balanced deal with local partners was not possible. There are often disputes about the rights of each party. Even when a negotiated agreement has been reached with local partners, enforcement as well as renegotiation has been difficult. The judicial process in the PRC is cumbersome and time consuming.”

**Operational and Financial Risks.** “Small and medium enterprises (SMEs) lack operational and financial management skills. Due to the existence of a myriad of receivables among businesses, the ability to collect receivables has been limited. In the absence of collateral that banks can foreclose on, accessing banks for needed credit has been extremely difficult for SMEs. The capital market is not sufficiently developed to provide alternative financing for SMEs. Therefore, joint venture SMEs tend to rely solely on foreign investors to provide cash.”

**Divestment Risks.** “Exit avenues may exist in the form of exercising a put option to local partners, trade sales to existing and other investors, and public listing at a stock exchange. Stock exchange listing is not easy for small size corporations, and even if allowed, listing in the “A” share markets has constraints for divestment by foreign shareholders. In addition, existence of adequate liquidity of the shares being traded is critical for divestment of a relatively large number of shares.”

**Information Disclosure.** “Obtaining “full” disclosure of information is difficult and the accuracy of information obtained is suspect. In addition to fraudulent practices in some business and financial sectors, full disclosure and transparency sometimes take a backseat to a notion of effectiveness.”

**Budget and Control.** “Business and budget plans are often set too aggressively to be achievable. There are lapses in the control function.”

**Inactive Board.** “Board documents are usually distributed late, and board discussions are not active. Often the board minutes are not complete and timely for effective reviews by board members.”

Box 12:

### Fujian Pacific Electronic Company Ltd. (Meizouwan) Project

As part of the restructuring of the power sector, the State Power Corporation (SPC) was formed in 1996 to, among others, place power assets previously owned by the Government into provincial subsidiaries, including the Fujian Power Company (the off-taker). The State Economic Trade Commission (SETC) gradually took over the regulatory and oversight functions of the Ministry of Electric Power.

The State Development Planning Commission (SDPC) cleared the Meizhouwan Power Project as a wholly owned project and in February 1998 ADB approved a loan for the 724 megawatt (MW), coal-fired project. Construction began immediately thereafter. The borrower and the equity and loan participants signed the financing agreements in May and loans were drawn beginning in October 1998. That a project of this size managed these milestones during the Asian financial crisis is due to what all agreed in 1997–1998 were solid economic fundamentals. The Project received two awards from international finance magazines and became a case study at Stanford University and Columbia University business schools.

Sponsors approached ADB in 1995. ADB led the due diligence and negotiations and participated in detailed project and loan document reviews. The power purchase agreement (PPA) was negotiated primarily during 1996–1997. Under the PPA, the Fujian Province assumed the risk should the power demand of Fujian not materialize. The PPA provides for a minimum off-take of the borrower of 5,000 hours. The Province wanted a short depreciation period (7 years) for the plant, which is partly responsible for the high tariff. SDPC approved the project twice during the 1990s. The second SDPC approval, required by ADB, states that the Project budget is \$655.3 million and that the average tariff during the debt service period is CNY0.517, and thereafter CNY0.464.

ADB was uncertain about the effect of the 1996 PRC Electric Power Law, which requires the tariff to be finally approved upon commercial operation by the department in charge of price control under the State Council. Just before going to the Board, ADB checked on the tariff clearance mechanism one last time with SDPC, but although some oral assurances were provided, SDPC declined to formally review the matter.

In 2001, the power situation in the Province changed from a power shortage to oversupply. During 1997–2000, while the economic growth in the Province slowed, the installed generation capacity in the Province increased following the Province's aggressive power expansive plan that included the 3,600 MW Hou Shi Power Project. The power oversupply is currently projected to last until 2005. Due to the oversupply, the Province became concerned about the economic impact of purchasing power from Meizhouwan, which would be the most expensive in the Province. The Province insisted that the borrower lower the tariff by reducing operational and capital costs and returns on investors' investments and challenged operations on technical grounds. Although initial discussions to resolve the technical disagreements failed and the Province made a decision to shut down the second unit in September 2001, ADB facilitated further discussions that led to the Province's decision to bring the second unit back into operation in January 2002. Technical disagreements have not yet been resolved.