



Financing and Managing Risks in Public-Private Partnerships (PPPs) at National and Sub-national Government Levels

Training Program ~ 21 – 27 October 2009

Academic Coordinator's Daily Concluding Comments

Mr Ken Waller

Day 1

- We started with an overview and reviewed key concepts that underpin PPPs
- Priority areas were assessed and we discussed why some PPPs are particularly attractive to the private sector and why others are less so – we noted that size and scale of PPPs are important to attract private investment, as well as a solid pipeline of activities
- We reviewed the institutional structures relating to the development of PPPs in an economy
- The country presentations pointed to a range of approaches and highlighted some similarities in the way governments develop and implement PPPs
- The roles of national and sub-regional levels of government differed across economies, reflecting governmental, constitutional structures and the power that resided in various levels of government in accessing and distributing taxation across an economy
- We considered the economic arguments for PPPs – we took as an example, the contribution that PPPs could and do make to support enhanced efficiency in external trade and the linkages between GDP growth and export growth, facilitated by solid infrastructure in transport, cargo handling, port facilities and so forth
- Managing risk sharing between the public and private sectors was considered and how governments had developed various funding approaches to provide for the public contribution; some had established special funds, particularly as a response to the global financial crisis; attracting private capital –both domestic and external – was a challenge at this time in the crisis
- An important issue for private investors was the certainty of a pipe-line of PPPs and the value of a having a minister as a “champion” of the concept was seen as very important in promoting community support and acceptance of PPPs
- It was noted that the PPP market is global and that private investors do have choices; what matters to the private sector is the pipeline, fairness in sharing risk and sound financing underpinnings; the private sector looked for transparency, accountability, predictability and a clear understanding of performance requirements and clarity in what governments want and expect from a PPP

- Emphasis was placed on the transactions nature of PPPs – it is the transaction that defines the project, the risk sharing and the financing underpinnings
- Defining the private sector is important in some economies where state owned enterprises and corporations have some characteristics of private operations but which receive government financial support
- Ensuring that governments fully account for contingent liabilities inherent in risk sharing in PPPs was seen as very important and uncertainties in whether comprehensive accounting is undertaken by governments on their PPP liabilities was noted

Day 2

- Based on its experiences in Vietnam, the World Bank noted the importance of setting up a PPP unit early in the development process and the relevance of agreeing a road-map on strategy, including funding; it was noted that getting things done was critical to development even though the law may not always be clearly enunciated
- APEC was involved in developing guidelines that may be helpful to ministers in responding to the global financial crisis and its focus is on enhancing efficiencies through measures that might improve bidding processes, bundling, and others aspects of PPP contracts and on best practices; it was noted that a principle of best practice was to turn “how to do” to “what to do”
- We considered that the focus for governments should be determining local domestic priorities in building the pipeline of PPPs
- While securitisation had become somewhat tarnished in the context of the global financial crisis, it remained an important financing tool in the dispersion of risk in relevant aspects of PPP financing arrangements
- We noted that rapid urbanisation was a key driver of PPPs
- While banks presently confront funding difficulties with a natural emphasis on deposits, financial sector specialists noted their expectation of a return to wholesale funding by banks; mono line insurers that had insured the bond market had disappeared as a class in the financial system and as a consequence the bond market had also closed; the crisis had led to “club” deal arrangements between selected banks and this had led to more costly funding and shorter debt structures
- The value proposition for PPPs had been seriously affected by the GFC – private sector financiers were not willing to take on the refinancing risk and this had changed the market dynamics with governments having to assume more risk sharing if a PPP was to go ahead
- Notwithstanding the problems associated with the global financial crisis, the fundamental reasons for PPPs remained and the GFC had demonstrated the robustness of PPP models; conditions however were now changing as premiums were coming down and debt tenors were increasing
- A comparison of macro-economic factors of India and China by the ADB concluded that options for the revenue base for public financing of PPPs and other expenditures showed that the most effective in terms of contributing to output growth and welfare in India was a consumption tax, in preference to either direct taxes on income or debt; it was noted

that over the long-term of a PPP, debt was an important burden that governments needed to be concerned with

- The massive growth of Islamic finance was discussed and aspects of Shari-ah law that might impact on PPP contracts in jurisdictions based on western legal principles
- A key aspect of Australia's approach to PPPs was "value for money" and that a framework had now been established agreed by the Commonwealth and State governments to facilitate PPPs; issues under consideration in Australia were bid costs and ensuring probity in dealings
- "Affordability" was seen as particularly relevant to governments in determining the PPP pipeline and how to manage the cross-generational issue of the public financing contribution to PPPs

Day 3

- Policy in Australia in developing Infrastructure Australia reflected the need to provide national leadership in freight and public transport; roads, rail and ports had not been developed on sound market principles and as a consequence there was a need to address market failures in terms of productivity and efficiency and investment and reforms
- Concerns have arisen in Australia about toll roads and the quality of forecasting traffic volume; ways in which national governments might utilise monitoring to provide incentives to sub-regional levels of government in promoting PPPs were noted
- A key constraint in PPP at lower levels of government was that of human resource capacities and often the inability of sub-regional levels of government to access financial markets
- The need to consider cross-border PPPs and how they might be organised was raised and that these activities clearly need government to government collaboration
- Bidding processes were discussed and differences noted in the way in which Mexico and Victoria dealt with applications and the criteria on which successful bidders were determined
- It was noted that the GFC had led governments to review the fundamental impact of the crisis on risk allocations and the increase in the amounts of capital or equity that governments needed to contribute to PPPs
- It was noted that in the light of changed circumstances, sharing of both future profits and losses had to be taken into account and that both governments and the private sector needed to be flexible in concluding PPPs arrangements
- We discussed China's approach to PPPs and noted that while China has no general PPP policy, many major projects are undertaken on a case-by-case basis and involving many agencies of the state and provincial governments
- The ADBI noted its plan to convene a forum in early December to consider a PPP country readiness index which would focus on country comparisons of policy arrangements for PPPs and procurement practices; around 30 country case studies would be included in the index and participants to the training program were invited to submit case studies on successes and failures and lessons learned

- Regional perspectives on PPP developments and with a focus on national and sub-regional levels of government were presented by Vietnam, the Philippines, China, India and Mexico
- Unsurprisingly governments have different approaches as to the policy structures in place and the efficacy of the impact of those approaches; we discussed the standardisation of documentation, the impact of GFC on financing and responses, contrasts between mega-bundling of major projects and community road-building projects in Vietnam, bidding processes and selection and the role of “shadow tolls, the complexities of forecasting road usage, ways to deal with windfall profits (and losses), dealing with unsolicited proposals and maintaining government priorities and ensuring the bankability of projects.

Day 4 – Workshops

Day 5 – Weekend

Day 6

- Presentations focused on an effective framework for PPPs as seen mainly by private sector practitioners and transactions specialists: issues covered included the financial environment, relationships over the long-term as a PPP is managed and operated; accountability and transparency in bidding; the legal framework and risk management
- One speaker noted that the current most important issue on financing is tenor of debt and the need of the private financier to have flexibility in approaches as a consequence of the GFC
- Uncertainty about finance and the high risk premiums now current required that the period between a bid and closure needed to be as short as possible
- Governments needed to consider options equity involvement
- The GFC had reduced the number of classes of PPP private sector originators in the Australian market and this compared unfavourably with the large number of institutions which would eventually be owners of a particularly investment
- Financiers/originators entered markets in different ways and a prominent Australian institution noted that it developed its strategy through entering into a market with a local partner; it did not rule out investing in sub-investment grade regions/investments if it could be assured of attracting solid backers and the deal was seen as solid
- Key issues for a financier are certainty of time lines; clarity of the project brief; scope for innovation, consistency in documentation and risk allocation – these will drive bidders to invest in high-risk and cost tender processes but the reality is that bidding is attractive to only a few sophisticated risk takers.
- The emphasis on the right people to manage and operate a PPP was seen as crucial; a contract is one thing but for the private operator the question is having or acquiring the right skills and experience to manage a project over its life-time; maintaining the whole of life quality of the asset was seen as critically important

- Not discouraging unsolicited PPP offers may make a market more competitive but there was a need to ensure that unsolicited offers comply with the priorities established by governments and if they are received, that they comply with the processes by which bids are determined
- It was noted that Mexico organises road shows to demonstrate to potential overseas and domestic organisers and financiers the government's proposals for PPPs and its processes
- The Victorian government has adopted the "Gateway" Initiative which sets out the objectives that a PPP project will need to meet before it can be approved as a project and provides for independent reviews at six key decisions points in a project's life cycle; importantly, a public interest test is applied to the assessment of each project; the Auditor General of the state provides an independent assessment of projects and financial reports are prepared on accrual accounting standards basis
- Bid processes are open and accountable and various legislative requirements in Victoria are aimed at ensuring accountability and transparency in PPP dealings; the value for money concept is judged against the whole of the outcomes the government seeks to achieve across its policy framework; probity has no particular legal meaning but describes the circumstances in which matters are being conducted – properly or improperly – and may be regarded as a quality required by and of government when engaging with the private sector
- While mono line insurers which absorbed risk have all but disappeared from financial markets, Export Credit Agencies and other agencies which provides for States' to guarantee finance, and the international financial institutions, are possible candidates to fill the space vacated by the insurers
- We discussed the environment aspects of PPPs noting that governments require PPPs to meet environment tests and we discussed responsibilities when projects may be damaged by earthquakes and other natural phenomena
- Key lessons from the Day included the view that the GFC had caused significant changes in the philosophy of the approach to PPS causing much greater emphasis on sustainable financial forecasts and the need for robust "change" mechanisms, changes to payments arrangements and to modes of risk transfer with the private sector.

Day 7

- First, I would like to thank you for the presentations made by the five working groups; they were of the highest quality and as you noted they provoked a really informed discussion with the panel; I share the panel's views about the detail that went into your deliberations in the working groups and the clarity of your thinking as expressed in the presentations
- I take the opportunity to thank the facilitators of each working group, Elaine Glennie of ADBI, Rory Allan, Arthur Smith and Kylee Anastasi. I particularly wish to thank the ADBI for their financial support for this training program and for personal support that Elaine has provided in the course itself
- Your written and oral comments on the concept of developing a regional register of PPPs are deeply appreciated; while some of you noted that data on PPPs is available on some

web-sites, you also noted that if a register was housed in a centre which had a capacity building focus and could assist in training and in distilling information about the PPP environment, it could contribute to regional development

- The key messages you have just provided about the course and the ideas and views we have discussed over the last few days were highly informative; you commended the quality of the exchanges we have had and a number of you advised some important matters you would wish to pursue on your return to your agencies; I sense we have learned a lot from each other, about the various approaches undertaken in each economy, the tools being used and the challenges that flow from the global financial crisis

Concluding comments

- I hope that the training course has fulfilled your expectation; in my view the presentations have been of the highest quality and the discussions we have had have been rich in detail and have covered both public and private sector considerations; the group presentations this morning were excellent and great credit goes to all participants for your work on the course
- In summarising, I would note that there are many pressures on governments, arising from:
 - Technological revolutions and innovations and which, inter alia, raise peoples' expectations
 - Demographic changes; the impact of growth strategies and policy options, including taxation, pensions, education and health and the GFC
- The GFC has forced us to think about changes to the ways we think about PPPs and risk allocation and relationships between governments and private sector partners
- These changes require governments to accept that greater equity participation in projects is more likely to be necessary and that the changing financial environment needs to be reflected in the contractual relationships between governments and the private sector
- The GFC has caused changes to the financial market dynamics of PPPs, including the demise of a class of mono insurers but the space they filled may become occupied by export credit agencies and other governmental and multilateral agencies
- Much shorter debt tenors and constraints on finance availability force private sector participants to seek not only greater equity participation by governments in PPPs but also acceptance by governments that they may have to underwrite debt refinancing arrangements (as occurred in the Victorian desalination project)
- We should also reflect on the fact that future finance availability may not be the same as it is now; conditions may improve over the next five years but they could worsen through unforeseen factors affecting energy, food, climate or for other reasons; it may therefore be prudent to review contractual clauses in PPPs with a view to building in more flexibility to allow governments and private sector partners the exercise of sensible responses to changing circumstances and to facilitate the completion of contracts over the long term
- The issue of contingent liability is very important; some governments have clearly established processes in place to accurately reflect government liabilities and these

usually involve a central reporting unit in a finance department or treasury and transparent reporting in budgets and in other official records; knowing the contingent liability and its consequences is part of the process of informing the public and in gaining community support for PPPs

- Governments' reputation can be at serious risk if PPPs fail to meet their objectives or if the public is confused about objectives and concerned that there is no clear accountability as PPPs are entered into and as they are effected
- People matter greatly in the administration and implementation of PPPs over the life of a PPP and there is an obligation on both governments and the private sector to secure and protect an asset over the whole of its life; good governance is paramount in both sectors in ensuring that good quality people with integrity are appointed to manage and administer projects
- Sound documentation and processes are important aspects of probity in PPPs and for ensuring that communities receive value for money.

I thank you all most sincerely for the quality of your input into your presentations and into the discussions that followed each session. We all agree that PPPs are an essential part of the development process and I sincerely hope that the experiences we have shared so comprehensively over the last seven days will be most valuable to you as you return to your agencies.

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