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Conditions Necessary for Successful Road PPPs in Today's Market

Henri CHUA

- IM Technologies Limited, U.K.
- Director
- henrichua@imtechnologies.co.uk



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IM Technologies Ltd,
a boutique transport
advisory with global
project experience

Introduction

- Henri Chua
- Chair of Technical Committee A.2 Financing, Managing and Contracting Road System Investment 2008-2011
- Director of IM Technologies Ltd, United Kingdom
- IM Technologies is a boutique transport advisory with global PPP project experience in 18 countries from Australia to the Americas, including Mexico, with a combined value in excess of US\$ 30 billion



The PPP Story So Far

- Early road PPPs are now teenagers and indeed by this time at the next WRA Congress in Korea some projects will be almost seniors reaching the gateway to handback
- Many early winners with some setbacks, typically project specific, so the whole can be considered a success and PPP an extra instrument in the road services delivery toolkit
- More road authorities, particularly from the emerging economies, are increasingly employing this delivery technique
- Just as the PPP party got into full swing we had a (near) global financial and economic meltdown
- Some early PPP adopters took supportive actions to assist PPP projects as we heard earlier this afternoon



Backcloth

- Too many PPP road projects, particularly real user toll ones, have under performed, in some cases appearing to be systemic
- Many public promoters are financially on the back foot
- Many road users are also financially stressed
- Many construction orientated sponsors have less equity capital but need more work
- Equity finance continues to attract new players although some earlier participants have become shy
- Critically, post the 2007 “go-go days”, debt financing has become “clubby”, more scarce, smaller, shorter and pricier



What is Success? Market or Markets?

- PPP still has a future albeit on a modified path
- The title of the presentation is *Conditions Necessary for Successful Road PPPs in Today's Market*
- But what is *success*?
 - *Success* should not be measured by financial close alone
 - But to include project and programme sustainability
- Also is it a single *market* or are there many different *markets*?
 - Numerous *markets* requiring varying considerations



Reminder

- More than ever what PPP is and is not need to be fully understood by all stakeholders
 - PPP is NOT alchemy to produce “free lunch” for some stakeholders
 - Nor a private equity asset class; expected rates of return need to be more realistic
 - A PPP is a long term service contract which can yield better value for money and expected services to tax payers/users as well as provide investors with reasonably steady incomes to match liabilities for a long period



Challenge

- Sources of Finance – urgent actions to widen and deepen financing sources are critical for road PPPs
 - Monoline insurers which provided long bond financing need to be “re-invented” perhaps with a different ownership structure involving sovereign wealth funds and multi-lateral financial institutions
 - IFIs need to up their co-financing activities; increasing volume and size of debt, equity and credit enhancement



New Recipe? 1

- Business Case – has to be strong and capable of withstanding rigorous stress testing
 - Strong economic fundamentals
 - Affordable
 - Genuine value for money
- Scope and Scale – has to be realistic
 - Small-medium size (millions not billions)
 - Fit-for-purpose rather gold-plated trophy specifications, importantly keeping them simple
 - Operation and maintenance focussed



New Recipe? 2

- Payment Mechanism – has to aim to minimise contingent liabilities to the public sector but bankable
 - In decreasing order of desirability: real user tolling, shadow tolling, lane availability and upfront subsidy
 - Monetise non-financial benefits into secondary shadow tolling and/or safety performance payment streams
- Risk Transfer – revenue risk transfer needs updating
 - “Cap and collar” sharing will likely be more appropriate than outright transfer of traffic GROWTH risk
 - However OPENING traffic levels as well as construction and completion risks should be business as usual



New Recipe? 3

- Procurement – simplicity and practicality are vital for success
 - Adequate time for comprehensive project preparation is crucial
 - Better to keep the exercise simple, avoiding any unnecessary complexities, such as separate financing competition
- Due Diligence – more needs to be done
 - Public sector must stress test offers and not just pick the “lowest price” offer
 - Lenders not sponsors should drive the process
 - Much more effort on traffic and revenue forecasts



New Recipe? 4

- Governance – the protection of public interests needs to be seen to be carried out
 - Perhaps to include, say, 1-2 independent directors on the Board of the PPP concessionaire company
- Help - if required, public sector should hire advisors
 - With strong individual staff (rather than corporate) performance and experience
 - Not on upfront price (90:10 preferable to 70:30 quality:price criteria)
 - Because poor to average quality advice could be very costly later



Thank You for Your Attention

