THE ADVISORY GROUP ON APEC
FINANCIAL SYSTEM CAPACITY-BUILDING

A Public-Private Sector Initiative

PUBLIC PRIVATE PARTNERSHIPS FORUM REPORT

Prepared by the Australian APEC Study Centre at RMIT University
15th February 2010.

Introduction

The Forum and an associated workshop were convened to further APEC's work in promoting PPPs in infrastructure in the region and to consider the idea of an Asia Pacific Public-Private Infrastructure Partnership (APIP). The latter would bring together public and private sector interests, multilateral agencies, academics and professional groups. It would assemble knowledge and information, address issues of asymmetry of information and support and promote capacity building.

Invitations to both the Forum and to the workshop were distributed widely through ABAC and the Advisory Group connections and to groups known to the Australian APEC Study Centre at RMIT University. The Centre convened the events in cooperation with ABAC and the Advisory Group and with Corrs Chambers Westgarth, Lawyers, Melbourne, which hosted the Forum, a lunch and a reception.

.

The background to the Forum and workshop and the programs are attached to this report, together with a list of participants. A separate report on the workshop will be circulated.

The Forum – 9th February

The forum was well attended; over 60 participants attended, drawn from business, public sectors, the Asian Development Bank, academia and professional groups involved in PPP design, administration, financing and management.

Mr. John Denton, ABAC member Australia hosted the Forum which was preceded by lunch. Mr. Tony Canavan, Director, Partnerships Victoria gave the opening address. He noted that

Australia was relatively well placed to manage the impact of the global financial crisis but that well before the crisis Australia invested heavily in infrastructure. Victoria has led the way in Australia in committing to developing its infrastructure through PPPs and the private sector is playing a crucial role in the process, including importantly in financing. He outlined the key processes in the development of guidelines and procedures and in knowledge sharing in the region. He responded to questions on managing the impact on the environment of PPPs and on work in developing a long-term pipeline of projects.

Session 2 considered prevailing market conditions for PPP contracts

In introducing the session, the Chairman, Mr. Mark Johnson noted that the Asia-Pacific Infrastructure Partnership was a model that the region could aspire to achieve. He observed that the Forum was designed to consider how best a model might be constructed, taking into account prevailing market issues confronting PPPs.

Presenters noted the need to look ahead beyond the global financial crisis. The appetite for risk is beginning to improve but the crisis heightened risk and there are long-term changes to the debt market. There is greater sensitivity to market disruption and a focus on which groups might guarantee against risk. In Australia, there is a push for a more comprehensive approach and a growing recognition of the need for PPPs to operate on an equity basis. There are limits to how much infrastructure can be built and a need to fit projects into broader planning. Taxation policy should focus on economic efficiency.

While the financial crisis did have an impact, governments have reacted and projects had been successfully transacted.

As regards developments in Japan, it was noted that in the past the public sector led the construction of infrastructure. Companies had experience in PPPs in the domestic market but were now focusing on operational aspects of PPPs. The new government is now focusing on growth frontiers and business involvement through technology and know-how. With a declining population, deeper investment in innovation and technology is a crucial aspect of Japan's development. There is considerable cooperation between Japan and India in a major transportation corridor. An Indian Minister had noted that this decade will be the "Infrastructure Decade".

Thailand is considering how to get out of an infrastructure mess. The country has the need, the will and the money but few PPPs are proceeding. There are political issues regarding concessions in PPPs to private operators. Changes in governments have tended to discourage private investment. There are limits on private equity in Thailand and on foreign ownership and all projects need to be at least 51% Thai owned. Thought is being given to establishing a private investment fund offshore in the hope that this would encourage private capital into the PPP space.

The Forum was advised that Colombia is involved in PECC and would like to be part of APEC and the dynamic Asia Pacific group. Opportunities to invest in Latin America should not be ignored. Brazil, Chile, Colombia, Peru and Mexico have infrastructure needs. Companies in Australia and in Asia are well placed to support Latin American economic development.

Session 3 considered measures by regional and global financial institutions to address impediments to PPPs, particularly in risk bearing and financing

Japan's Bank for International Cooperation provides loans and guarantees. Its representative noted that risk sharing needed to be economically feasible and financially viable and that risks should be allocated to the party best suited to bearing risk. For any risk sharing, government commitment to a project is essential. Host governments needed to provide commitment, a stable policy, legal and regulatory framework and sound environmental and social policies. Currency convertibility is a prerequisite in attracting foreign capital, as is a right to remit funds. The tendency for host governments to push risk onto the private sector is to be avoided, as are overly optimistic assumptions for demand projections. Governments should allow for flexibility to adjust arrangements and mechanisms should be agreed with the private sector.

The Asian Development Bank takes a bottom up approach in looking at PPP transactions. Sovereign risk is an issue in some economies even where a project might appear to be soundly constructed. Commercial banks support economies they know and have experience with. However, international banks and local commercial banks are coming back into PPP financing. The ADB 's AAA rating means that through associating with a project the ADB can provide confidence to private sector participants. However, the guarantees available from both the ADB and the World Bank are under- utilized. The ADB has provided guarantees on political risk in projects in Afghanistan and this demonstrates a capacity to get projects implemented.

The ADB has the capacity to do a lot more in PPP infrastructure and finance is available. However, frameworks to transact PPPs need to be in place. Longer-term, it will be important to fund infrastructure from local savings. Self -assessments by economies on their capacity to undertake PPP projects suggests that a number have unrealistic expectations about their preparedness to implement projects. In these situations, the ADB will work, through its various facilities, to encourage private sector involvement in PPPs.

An Australian private sector specialist noted that not enough is being done to attract funding into PPPs. The idea of a perfect match between public and private interests is an unlikely scenario and much rigour and work is required to bring this decade into the decade of "infrastructure PPPs" There is a large pool of finance and expertise in the region but there is a case now to build the relationships between all concerned parties.

In discussions, it was noted that optimism in forecasting should be avoided and that facilities are available to manage risk. Capital pools are available to finance PPPs but work is needed to bring long-terms savings pools in the region into infrastructure financing. Money is available but capital market structures are under-developed. Investors are less interested in PPP financing and attracting them remains a challenge. It was also observed that political support is a critical factor. An issue was raised on the need to incorporate in contracts the concept of risk-bearing over the life of a project and whether the tender procurement mode is the only mode, or whether other practices were relevant to some economies. The ADB's willingness to discuss financing arrangements with the private sector was favourably commented on.

Session 4 discussed the establishment of an institutional framework for an Asia-Pacific Infrastructure Partnership and an offer to support activities in Melbourne through 2010

In introducing the session, the chairman noted the various efforts in place in promoting PPPs and that a partnership needed to relate to PPPs at national level, sub-national and national level and sub-regional level, and involve public and private parties. The ADB is promoting various financial arrangements and seeking to address asymmetry in information as well as long-term financing requirements through a Pan Asia Infrastructure Forum. There are presently no counterpart groups in the private sector to match those of governments. APEC includes the largest economies and it has a mechanism for involving the private sector and an objective through ABAC is to deepen government/private sector relationships. Japan as chair of ABAC is supportive of an institutional partnership.

The co-chair of the Senior Officials' Meeting noted that APEC promoted regional efforts to further PPPs in the region and that Japan wished to work with ABAC to achieve that objective. A desalination plant under construction in Victoria involved Japanese and other private sector investors. Transport infrastructure would promote supply chain connectivity – another important APEC objective. A regional group would encourage private sector financing and support an expanding growth agenda.

As regards an APIP, it would be important to recognize that on some projects there could be cooperation between various parties but that others might benefit from a competitive approach. There would be a need to look at the unique strengths of each project and of each economy. Capital market mechanisms needed to be developed to generate the enormous capital required to finance infrastructure and to cooperate with government funds in project financing. Matching financing opportunities for projects is the key objective and there are now some guidelines in place. We need mechanisms to create projects and to reduce risks. Also needed is a facility to share best practices. APIP could further promote PPPs and while there is sound technical knowledge available, generating political will and appreciation would be relevant. Capacity training and education would also be important, including in the private sector.

It was noted that various parties needed to come together to make a partnership effective and that an institutional framework should contribute to resolving some of the many challenges in PPP development. Partnership between governments, the private sector, academics and researchers is critical and with its wide reach into Asia and Australia, RMIT University is well placed to support educational efforts which are relevant to PPPs. Education is an infrastructure investment for the future and that is why RMIT University supports the APEC Study Centre and the initiative at the heart of the Forum.

The Victorian government has dual objectives in PPPs. These cover industry involvement in developing PPPs and a financial interest in getting best value for money in PPPs in the State. PPPs are a strength for Victoria as an exporter of financial services and the development of PPPs helps position Melbourne as a global centre of excellence – also a Government goal – for training in financial services in the APEC region. Government support for the Melbourne APEC Finance Centre, a facility at the Australian APEC Study Centre at RMIT University, fits well with these priorities. Partnerships Victoria is internationally recognized as a specialist in PPP development and for its expertise.

It was noted that a private Japanese owned bank in Australia supported many PPP projects both pre and post the global financial crisis, and would continue to do so through loans and credit facilities. Whether in Australia or in overseas markets, documentation and legal risk is a challenge but if a bank can build and deliver services then governments would participate with banks in implementing PPPs. One impact of the financial crisis has been that financing is available for shorter periods – 7/9 years – compared with the pre-crisis environment. Currency issues also pose challenges for banks and regional PPPs require regional solutions.

The chairman of the session noted the strong support for the concept of a partnership arising from the discussions. He pointed to the relevance of the research and training and data collections to support regional PPPs and the network of institutions in this field that were active. He welcomed the lead taken by RMIT University and the State Government of Victoria noting that Victoria was a good place on which to build the initiative. There is a rich experience in PPPs and cross-border interest in infrastructure. Japan is entering a period where business and the government are looking at the Asian region to sustain growth. There is an opportunity now to address the many issues in promoting PPPs.

In discussions, participants noted the need to pay greater attention to the politics of PPPs. Tackling technical issues was important but political sensitivities on pricing was a critical aspect of gaining aspect of regional PPP development. Emphasis was placed on enhancing PPP activities to generate political support. Education at various levels was discussed. Education needed to be both at the "high" political end and at the technical level. Different approaches would be required. Dislocation was noted as a real problem arising from PPPs in smaller economies where private sector managers of projects drew scarce labour from other economic sectors.

In his summary conclusions of the Forum, Mr. Mark Johnson commended the engagement of participants and the high level of expertise that had been brought to the discussions. He observed that the Forum had discussed the big picture – PPPs as an APEC priority endorsed by Leaders, the massive funds involved and the fact that requirements are dynamic, reflecting changes arising from the impact of the global financial crisis and how these had impacted on models. He noted that dynamics of markets would cause further changes to models now being used.

The private sector is interested to participate in PPPs and looking for ways to mobilize funds, noting the risk profile of PPPs, the long-life and capital intensity and the fact that local currency revenue streams do not match private sector financing requirements. He observed that the role of the IFIs is pivotal. Structural adjustments were required to develop regional bond markets and ABAC and APEC are supporting those adjustments.

Harnessing the private sector knowledge and expertise was of concern to policy makers but the private sector would be responsive only if projects could be expected to make realistic returns. Ministers and public sector officials were attracted to PPPs only if they contributed to community growth and development. But resistance to engaging the private sector was an inhibiting factor in some economies.

The proposal for the APIP was useful. While the model is aspirational it would ultimately require solid commitments and financial and human resources. He asked whether participants saw a structure that fitted with a strategy and noted that a partnership should not seek to be a substitute for the ADB or the World Bank and nor should it be captive to private sector interests. He welcomed the participation of educators and academics as part of the institutional structure.