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INTRODUCTION TO PUBLIC PRIVATE PARTNERSHIPS (PPP)
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Agenda

Contact Details

Duncan Olde
Division Director
New Zealand
☎ +64 9 363 1413
✉ Duncan.Olde@macquarie.com



Public Private Partnerships

1

Public Private Partnerships

- PPPs refer to the partnering of the Government and private sector to work together in delivering infrastructure projects or services that are traditionally provided by Government
- Key features of a PPP structure:
  - Long term concession for the provision of infrastructure or services related to infrastructure
  - Output based specification
  - Private sector provides the infrastructure and may provide services
  - Public sector may provide core services
  - No revenue until infrastructure is operational
  - Public sector makes performance abateable service payments
  - Infrastructure returned to the public sector at end of concession for no cost
- Government retains a role in the project through:
  - Approval and supervision of the project
  - The Government may retain an operational role – e.g. hospitals
  - Availability-based payments
- PPPs are extensively used globally in transport, education, health, justice, defence, water and accommodation sectors

Why use a PPP structure?

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- PPPs have key advantages to the public sector including:
  - Value for money relative to risk adjusted whole of life cost to public sector (public sector comparator)
  - Risk transfer to private sector
  - Acceleration of delivery of infrastructure (but they are not simply a funding mechanism)
  - Forecasting and budgeting predictability through fixed pricing
  - Whole of life management
  - Innovation across all facets

Key PPP models

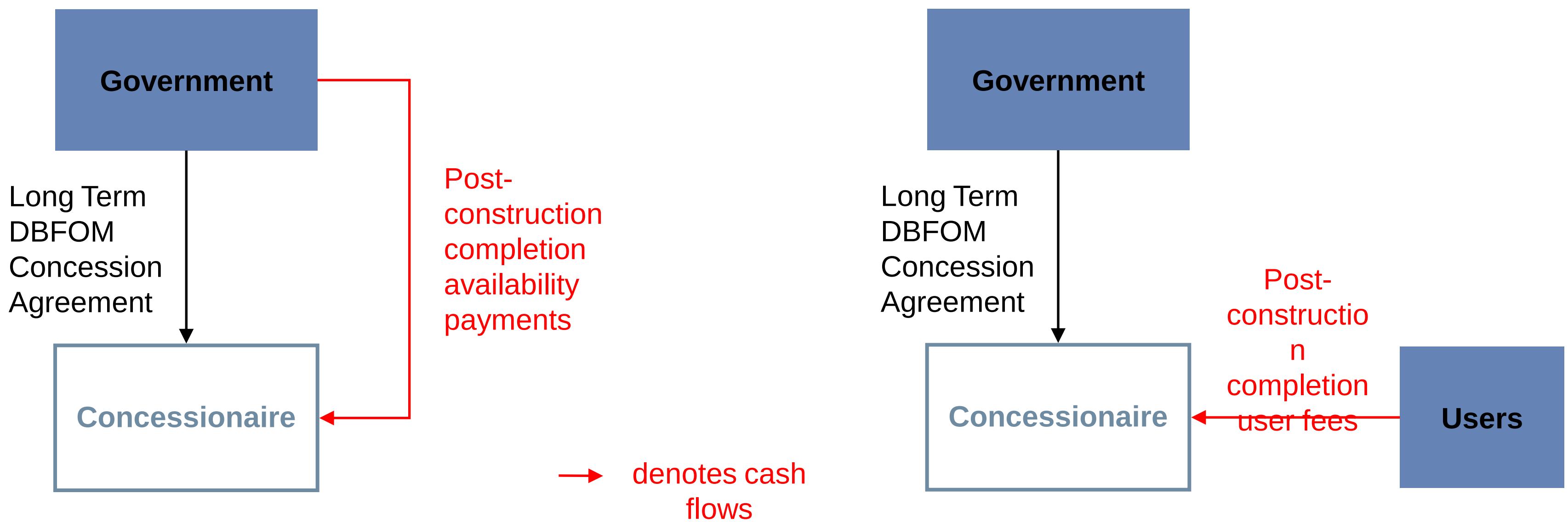
- Essential difference between the two key models is the transfer of demand risk and therefore the source of revenue
- Both are DBFOM models with a long term concession agreement

1. "Availability payment" based

- Availability payments can be abated for both failure to make the asset available and for failure to meet agreed KPIs
- 3rd party revenues may also be available

2. "Demand risk" based

- May also include KPI based penalty regime



Contractual structure

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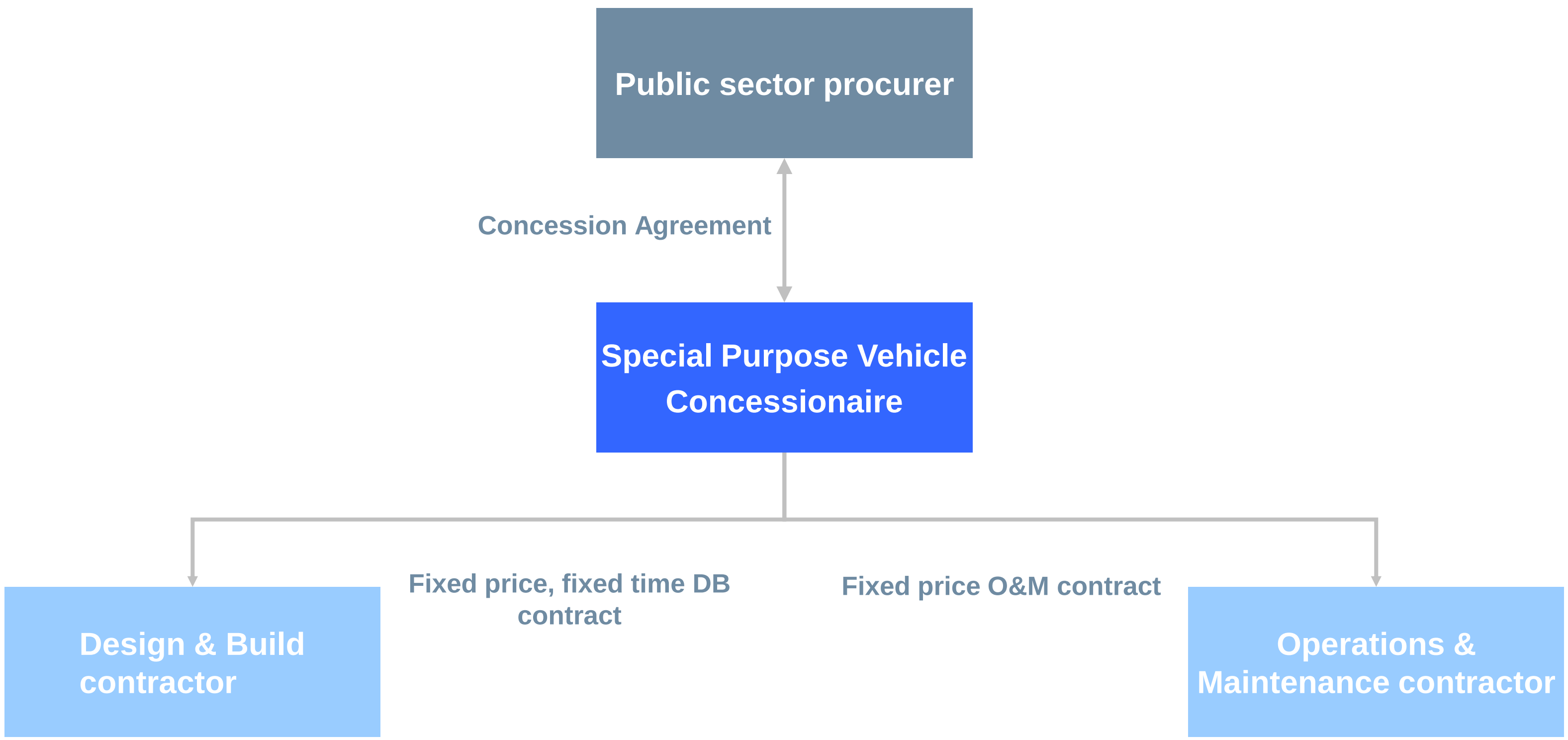
- The Concession Agreement includes design, build, finance, operate, and maintain obligations/risks
- Under a typical PPP contractual structure, the Concessionaire passes on risks to key sub-contractors



Consortium formation

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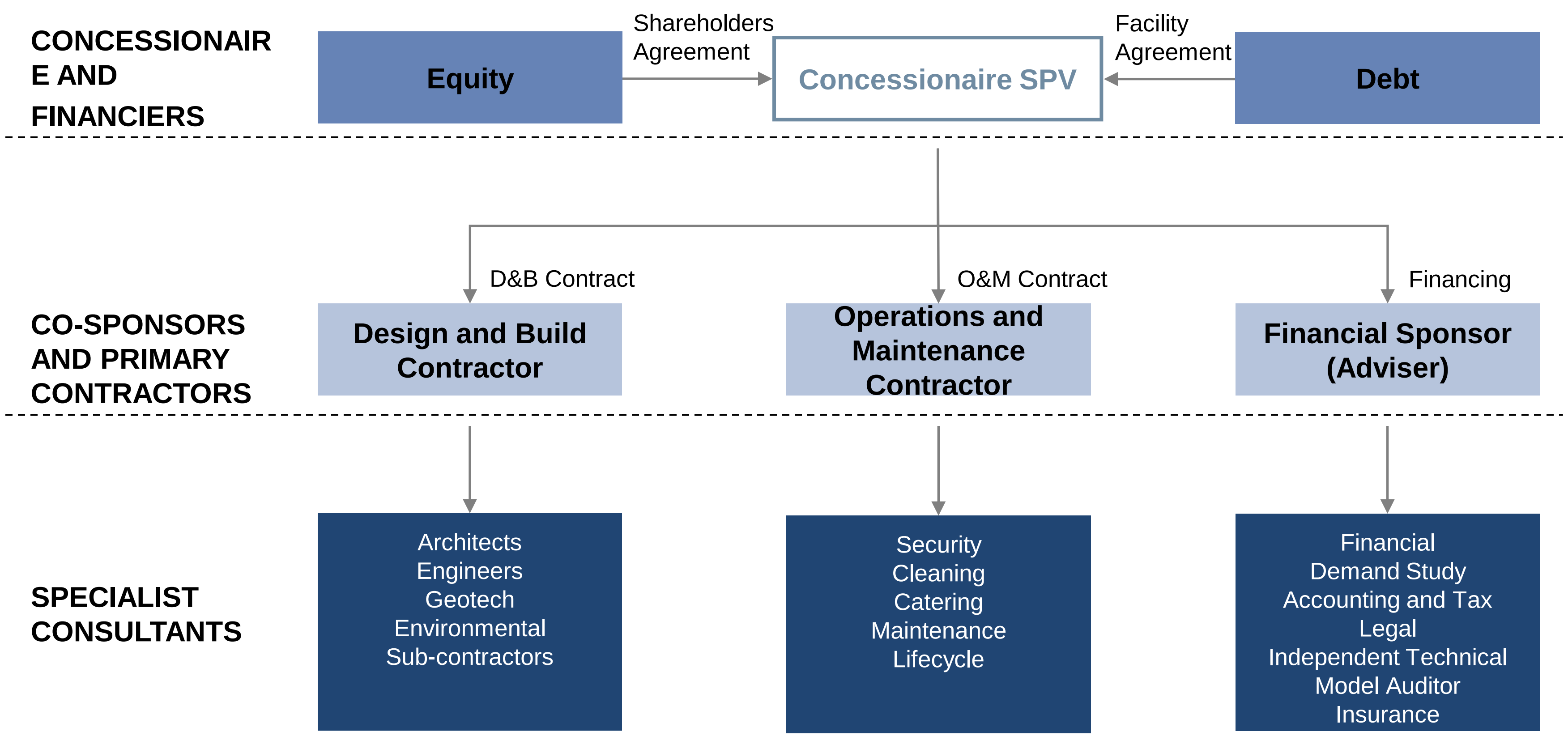
- PPPs involve a multitude of private sector disciplines



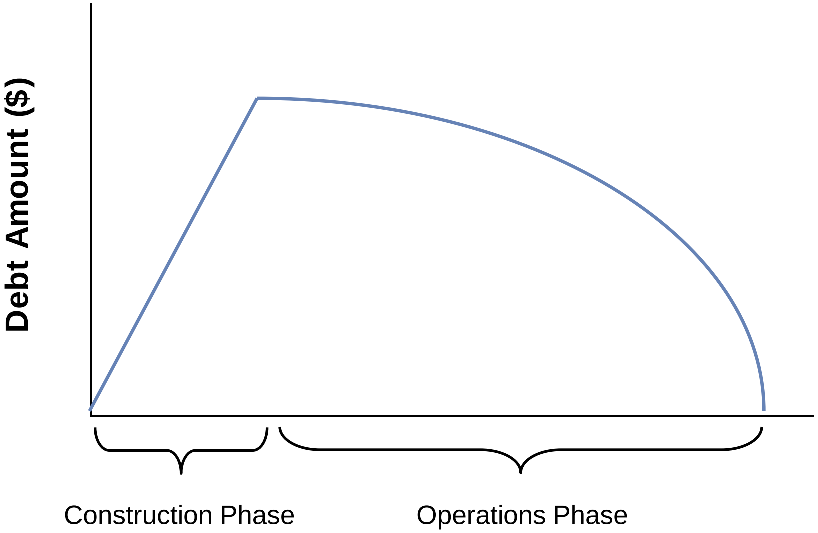
Typical PPP bid process

Public Sector	Private Sector
Project announcement	Consortium formation/consolidation
Market sounding	Market positioning
Request for Expressions of Interest (4 – 6 weeks)	Provision of high quality credentials based submission
Shortlisting of 3 consortia	Further teaming discussions
Request for Proposals (3 – 5 months)	Development of a fully underwritten documented DBFOM proposal
Bid evaluation/BAFO (1 – 2 months)	Response to questions
Preferred Tenderer announcement	Celebration/commiseration
Financial Close (1 – 2 months)	Completion of all key issues leading to contractual and financial commitment

Financing PPPs

- The global financial crisis had a significant impact on availability of credit
  - Markets have little appetite for greenfields PPP projects with demand risk
  - However, greenfields PPP projects structured with availability payments remain attractive
- Financiers undertake extensive and rigorous due diligence with key focus being on:
  - The public sector's obligation to pay (payment mechanism, compensation event regime, and termination event regime)
  - The pass through of risk to the sub-contractors (gaps analysis)
  - The sub-contractor's capacity to perform (security package)
- Financing metrics are improving post GFC
  - Debt ~ 80% - 90% of funding
  - Equity ~ 10% - 20% of funding
  - Pricing is also improving
- Funding is used to pay the D&C Contractor and other development costs
- Funding is repaid by availability payments over the life the concession

Debt profile over life of PPP



New Zealand Situation Update

2

Movement towards PPPs

New Zealand's historical experience with PPP is poor

- Historically, there had been strong opposition to PPPs, on the basis that many of the benefits could be delivered under more traditional procurement models
  - There are however a number of examples of contracts that include some of the key elements of fully fledged PPPs
- Track record for utilisation of PPP-like structures outside of Central Government has been poor with several failed processes

Improving New Zealand's infrastructure is a key Government priority

- Infrastructure investment has been falling in most areas of the New Zealand economy since the 1960s
- A leading campaign promise made by the National Party during the 2008 general elections was to increase spending on infrastructure
  - NZ$7.5b was set aside in the 2009 Budget for infrastructure spending over the next five years for roads, ultra-fast broadband, schools, hospitals, state housing, and rail

Steps are being taken to set up a working framework for national infrastructure

- Government has set up the National Infrastructure Unit (NIU) including a National Infrastructure Advisory Board
  - The NIU sits within Treasury and has released "The National Infrastructure Plan" which sets out a 20 year infrastructure plan including priority projects
  - The NIU is expected to work collaboratively with the relevant Ministry in procurement of new infrastructure

PPP opportunities by sector

Sector	PPP likelihood	Comments
Corrections	✓✓✓	— Government has announced that a new prison that will be New Zealand's first social infrastructure PPP (scope is DBFOM). Subject to further Cabinet approval, Request for EOI expected in early November. — Political pressure to solve both capacity and ongoing cost issues — Legislation passed to allow private sector operation of existing prisons – three responses to RFP for outsourcing of operations at Mt Eden.
High Speed Broadband	✓✓✓	— Strong political commitment to develop a national broadband network — Government is looking for private sector partners to invest alongside it to provide ultra fast broadband to 75% of New Zealand on an accelerated timetable — Parties have been shortlisted including Telecom NZ and various electricity lines companies
Education	✓✓✓	— Strong political will to use PPPs — Adviser appointed to undertake Stage 2 business case — Request for EOI could be issued in March 2011 — The tertiary sector is also a likely source of projects

PPP opportunities by sector

Sector	PPP likelihood	Comments
Roads	✓✓	— Some of the seven Roads of National Significance could be procured under a PPP model. The most likely candidates are: — Waikato Expressway — Transmission Gully — Puhoi to Wellsford — Likely to be procured as availability payment PPPs with any toll revenues for the benefit of the public sector
Healthcare	✓✓	— MoH has indicated willingness to consider PPPs — Individual DHBs are investigating and pursuing options — Potential tension with PPP model exists due to decentralised procurement model and changing models of care requiring infrastructure to be flexible — PPPs used extensively in healthcare in offshore markets
Defence	✓	— Defence Review launched in June 2009 in the face of resource pressures to gather public views on the direction of the New Zealand Defence Force — PPPs have been used overseas for defence housing projects — May see greater private sector involvement in short term funding of equipment

PPP opportunities by sector

Sector	PPP likelihood	Comments
Rail	✓	— The New Zealand rail sector has identified over $4b of capital for below-track and above-track projects over the next 5 years — Fragmented rail ownership, funding sources and responsibilities makes coordination for a centralised PPP difficult — Rail infrastructure projects lend themselves to a PPP style approach so may be some standalone projects
Water	✓	— Land and Water Forum report highlights some of the challenges faced by the industry. Reform is necessary to facilitate projects. — Long term capital plans for local councils show increasing funding requirements for water infrastructure — Scalability is a key issue given fragmentation of the industry with many local Government projects being small — 15 year restriction on concessions will be removed

Implications for Contractors

3

Key implications for contractors

- A Consortium not a contractor is required to win and deliver a PPP
  - Contractor need relationships with financial sponsors and O&M contractors
  - Teaming discussions occur early and are critical to a successful outcome
- PPP bids are more expensive than traditional design build bids
  - Proposal is comprehensive for all elements
  - NIU is conscious of avoiding the Australian experience in relation to bid costs
  - However, contractors are typically expected to cover the costs of consultants required to deliver the design build component of the proposal
- Financiers/Partners require transparency
  - Financiers will require detailed due diligence to be undertaken during the bid phase to determine that the price and program is both adequate and competitive, and that risks have been adequately mitigated
  - This will require a high level of disclosure in relation to pricing
- Fixed price and fixed time contracts are a pre-requisite
  - Contracts are robust and variations are the exception
  - Liquidated damages equivalent to foregone revenues for late delivery

Key implications for contractors

- Whole of life costs not construction costs are the key
  - Lowest build cost may not win
  - Key workstream involves all consortium players trading upfront costs against ongoing costs
- Financiers require significant financial support from contractors
  - Equity – skin in the game
  - Parent company guarantees
  - Security up to 10% of the value of the contract
  - High caps on limitations of liability
- Risk transfer is greater under PPP than traditional design build
  - E.g. in Australia, risks such as contamination and approvals are shared or transferred
  - Require the capacity to analyse, mitigate, and price risk
- Concessionaire SPV is the client and not the public authority
  - Concessionaire provides the funding so will require a voice
  - Need to work collaboratively and efficiently with the concessionaire