

Public Private Funding Potential


The private sector has a significant role to play in funding the country's infrastructure. Public-Private Partnerships or PPPs present the various stakeholders with the opportunity to determine what type of funding is suited to a particular project. The establishment of National Treasury's PPP unit has gone a long way to provide a framework to evaluate projects and in so doing, ensure service delivery, as well as value for money, risk transfer and affordability for the public sector.

The public sector may have resource and funding capacity constraints and can look to out-source such requirements to the private sector. This frees up the public sector so that it can focus its capacity on socially orientated projects while the private sector partners with the public sector in developing commercially viable concessions. PPPs help government to reduce the pressure on public finances but at the same time, provide essential public services.

The attractiveness of PPPs has to be in their promotion of genuine risk transfer to the private sector with projects contracted to be completed within a specified time and within a specified budget. Even more importantly, is the ongoing long-term delivery of services during the concession life of a PPP which ensure ongoing operations and maintenance of the state assets, with government getting a fully paid-up and upgraded asset at the end of the concession term. The private sector has to worry about the lifecycle costs and performance of the asset in order to get a return on investment. This has not always been a concern of the public sector.

The funding options for infrastructure are reflected in the funding continuum below. Management contracts would feature at the extreme left of this continuum while the full privatization option would be reflected on the extreme right, a slot to the right of concessioning.

Funding Continuum

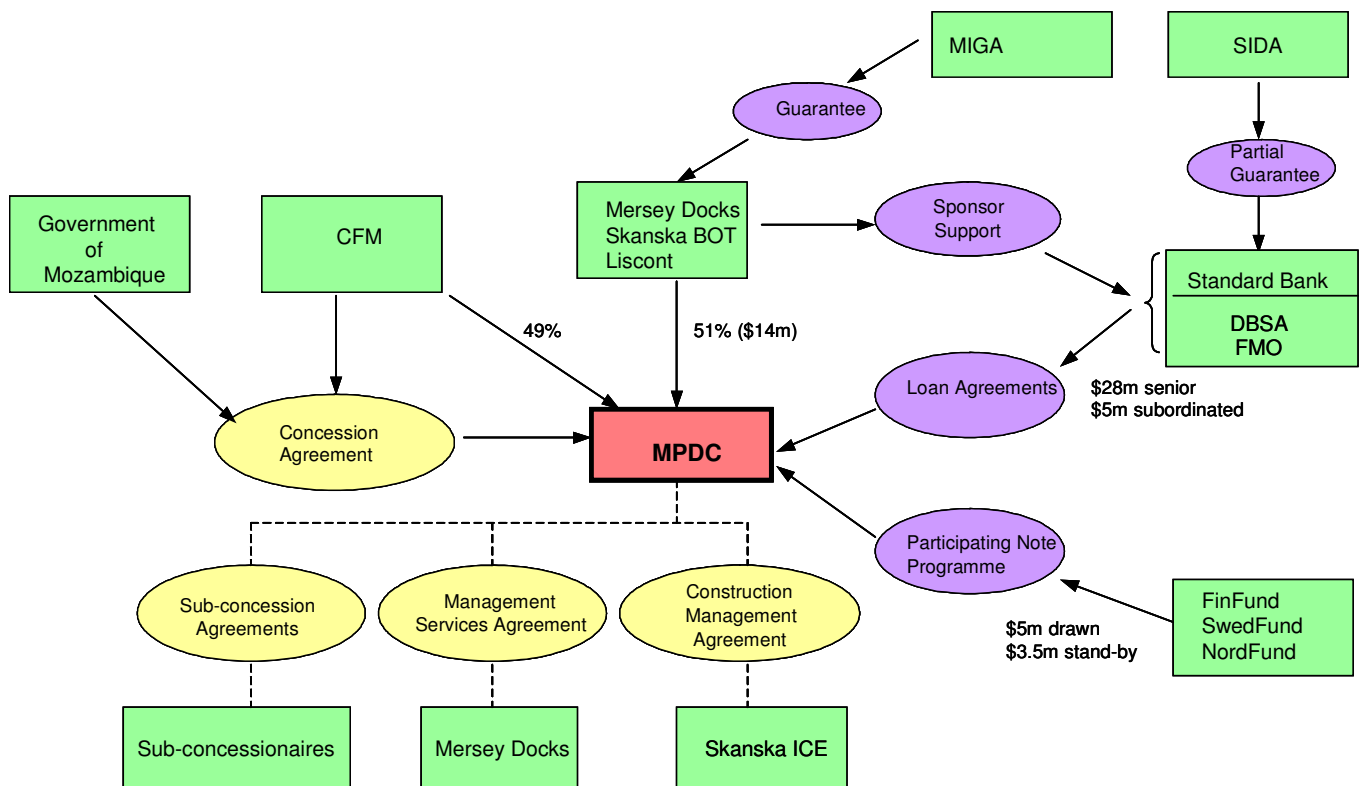


Corporate Lending/Bonds	Finance Leases	Operating Leases, Securitisation	Concessioning
On Balance Sheet, Impacts gearing ratios, Documentation/process un-complex	On balance sheet	Off balance sheet, docs and process more complex	Off balance sheet, no impact on gearing, conducive to empowerment, docs and process fairly complex,

When considering an appropriate funding structure, the cost of capital is most certainly a consideration. Private equity is typically more expensive than public funds but this has to be balanced with the value of risk transfer to the private

sector and the efficiencies that are likely to follow. There are many private sector funding sources in SA. These range from the commercial banks to the well-developed institutional or capital markets. Funding is available for tenors up to circa 22 years which bodes well for the long-term nature of infrastructure projects. Concession terms would typically exceed the anticipated debt term so as to allow a buffer over and above the contracted debt term. In certain African markets, where the local banking markets are not as developed as South Africa's, the requirement for longer tenors of debt becomes more possible with the involvement of development finance institutions who credit enhance the political and commercial risk for commercial lenders. Maputo Port is an example of such an arrangement.

Typical Port Concession Structure – Maputo Port:



The Big Concessions Debate

This leads us to the ongoing debate as to when (and how) to concession. We advised on and arranged finance for the first port concessioning in Africa, Maputo Port, so we can contribute to the debate. In considering whether to PPP/Concession or not, parastatals such as Transnet should be asking themselves certain questions.

In macro-economic terms what if concessioning the Durban Container Terminal (DCT) could result in better efficiencies and lower handling charges for industry? If the Net Present Value of these benefits to industry were greater than the loss of income to Transnet, wouldn't the economy be better off with concessioning? It's a big **if**, but there doesn't appear to have been an objective study done before the concessioning programme for DCT was shelved. It now appears that DCT and other existing terminals are unlikely to be concessioned, since they are seen as core assets of Transnet and termed "strategic".

There are other terminals in the pipeline, and concessioning will/already is featuring as a consideration:

- South Terminal, DBN
- Coega
- Car terminal (DBN, EL)

There are many reasons in favour of concessioning, to name but a few:

- Competition for existing operators (eg. DCT)
- Creating new capacity without further burden on Transnet's balance sheet.
- Leveraging third party capital e.g. Auto companies could invest in a car terminal, just like Kumba has offered to invest in the Orex line.

How can this be done?

The table below, which has been extracted from the World Bank Port Reform Tool Kit (Module 3, Box 6), provides a brief synopsis of the various port management models and the stakeholders' interests. The extreme type is that of full privatization where typically, as at certain ports in the UK, and in the absence of a port regulator, the privatized ports are self-regulating.

Basic Port Management Models				
Type	Infrastructure	Superstructure	Port Labour	Other Functions
Public Service Port	Public	Public	Public	Majority Public
Landlord Port	Public	Private	Private	Public/Private
Private Service Port	Private	Private	Private	Majority Private

A more 'balanced' approach is offered by the Landlord model or Landlord Port. This is a widely-used model that has a mixed public-private approach and that has been used for medium to larger-scale ports. In this example, the NPA would be the landlord and it would retain ownership of and responsibility for port infrastructure. It would also act as the regulatory authority. The NPA would fund the 'long-lived' infrastructure whereas the private sector operator's role would be limited to developing and funding the superstructure, equipment and systems, operations and cargo-handling. This role would typically require the operator to fund the building of warehouses, purchase and maintenance of cranes, etc.

In contrast to a management contract, the private sector investment as a result of the landlord model would help to ease the capital strain on Transnet. In addition, the NPA would also benefit by typically charging a concession fee or other relevant fee to the operator in return for the usage of the infrastructure.

Rotterdam, Antwerp and more recently, Singapore are examples of landlord ports. This model would require co-operation between the landlord and the private sector operator so as to effectively manage and co-ordinate infrastructure needs. The inland logistics are obviously critical to a successful port.

The attractiveness of this model is that it offers to the public sector, the expertise and innovation that is so widely seen in the port operations industry worldwide. The private sector operator is also generally better placed to cope with market requirements.

Certain port operators do also have interests in shipping lines and while this may foster integrated transport chains (and hence, competitive pricing), there is a concern that this may also promote monopolistic behaviour. As may also be the case with a public sector service port and a fully privatized port, monopolistic behaviour is not desirable and appropriate measures would need to be taken to guard against this.

Benefits of PPPs/Concessioning:

The bottom line is that Transnet and other government parastatals can introduce private sector capital and expertise by concessioning and still get a cashflow benefit e.g. via concession fees and royalties. With a proper evaluation of value-for-money and risk-transfer, the benefits to the country as a whole cannot be underplayed.

Labour interests cannot be ignored. In many jurisdictions, concerns vis-à-vis labour can be addressed by absorbing labour into concessions or retrained/redeployed as sub-contractors to the private sector concessionaire or utilized more generally in a port-wide pool of labour.

Private operators can bring new efficiencies and potentially new and innovative approaches to optimizing capacity/utilization of port assets, terminals and quays. Service and tariff levels would also typically improve with the improved efficiencies, benefiting the industry as a whole. Most private operators are highly disciplined in the manner with which they manage their operations by using the latest management concepts, software and professional staff to attain the highest possible efficiency levels. Property within the port area is another issue. Private operators are now focusing on identifying opportunities and developing solutions in order to maximize the value of its surplus port lands and create additional revenue streams and comparative advantages. Sub-concessions, for example, generate significant revenue for the Maputo Port concessionaire.

Lessons:

Probably one of the most important factors when considering the potential for private sector participation is how conducive the legislative framework is to private sector participation. The right institutional framework is key to promoting an efficient integration and alignment of private sector interests with those of the public sector. Without this, many hours, many years of frustration, can result with potentially lost revenue to all interested parties, including the fiscus.

As important is an enabling inter-modal and logistical environment. We have seen what financial impact a poor rail link has had on the viability of a port and the resultant impact on that country's economy (Maputo Port). In this case, it is fortunate that the road can provide a substitute for rail transport – however, the implication is that the road, and hence the user, will suffer as a result of the increased capacity and resultant additional road maintenance that will be required. Cross-border issues are also important especially where customs officials and border controls do not align themselves with the interest and needs of the private sector.

It should not be forgotten that concessioning/PPPs introduce an element of competition through the tendering process that takes place. By virtue of this competition, international operators and their funders all put their best foot forward to secure a role in developing a business or asset that is their area of expertise. The adjudicators of such a process are tasked with the responsibility of mandating these experts to look after their assets to the best of their ability, for the benefit of the country, while ensuring that such a partnership will be affordable for the public sector, generate value-for-money and transfer risk to those that can best manage it.

It is appropriate to conclude by quoting a paragraph from The World Bank Port Reform Tool Kit (Module 3):

“Experimentation in shifting the boundary line that divides the public and private sectors has resulted in a healthy pragmatism. Today, best practice is more concerned with results than with ideology, and is intended to result in:

- *Increased service levels for infrastructure users;*
- *Increased efficiency in operations; and*
- *Improved allocation of limited public funds.”*

Sources used: The World Bank Port Reform Tool Kit - Module 3