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Editorial

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EDITORIAL

Welcome to Edition 7 of the Public Infrastructure Bulletin. The two articles we feature in this edition are both refereed and deal with matters central to the future of public private partnerships (PPPs) in Australia – state participation in the debt finance facilities used to finance the transaction and the likely impact of volatility in capital markets on public private partnerships (PPPs) in this country.

Richard McKenzie is a Commercial Analyst with West Australian Treasury Corporation who has worked with the OECD in Paris. He has undertaken a comprehensive analysis of two approaches to public participation in PPP debt capitalisation. The first is the UK designed credit guarantee finance model (CGF) introduced in 2003/04 and trialled on two health projects in that country. The second is a model designed by Queensland Treasury Corporation and first employed on the South East Queensland Schools project. This is known as the supported debt model (SDM) and is different to CGF in that state participation commences on asset commissioning. There are significant differences between the two approaches although they both have the objective of reducing overall cost of capital and improving value for money. Richard explains the differences and examines the strengths and weaknesses of state provision of PPP debt.

The article highlights two important challenges to the wider implementation of the model in both jurisdictions. First, the state may lend senior debt to consortia as a percentage of overall capitalisation. This may increase the requirement for more expensive mezzanine and equity capital. This suggests that the window at which the consortia's average cost of capital is less may be narrow indeed. Second, the junior and mezzanine debt frequently provided by senior lenders at a higher coupon is no longer an option. Second, it is important to maintain a correct alignment of incentives which is necessary for optimal performance under the PPP procurement model. The role of syndicated lenders in the PPP operational hierarchy is important and little understood. Removal of that part of the formula may well lead to unintended consequences. Nevertheless, if private debt capital is difficult to source and spreads maintain their present levels, the new models may no longer be an option but a necessary feature of this method of procurement. This is a well researched and written article and we are very pleased to include it in this edition of the Bulletin.

Present capital market conditions are addressed in the second article which is based on a recent research report prepared for the Mirvac School of Sustainable Development at Bond University and the Infrastructure Association of Queensland. The data was sourced from a survey conducted in November 2008 of the major firms engaged in PPP and infrastructure finance and investment, fund managers, financial intermediaries and credit rating agencies. The survey suggests continued instability as risk is repriced in debt and equity markets for some time to come. However, the survey indicates that the PPP procurement model should survive and continue to evolve to meet changed market conditions. Nevertheless, several characteristics will change including approaches to risk allocation, patronage or market risk, the listing of immature assets and higher debt costs. The recent revised ratings of the credit guarantee providers also suggests problems ahead for the refinancing of existing assets over the next few years. An electronic version of the full report is available from the editor.

We'd like to hear from subscribers of the Bulletin and we have a standing invitation to anyone engaged in this industry to let us have their views or submit an article. Articles may be peer reviewed and we have a strong Editorial Committee to assist with this. I'm sure you will find this an interesting edition.

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