

The Impact of the Financial Crisis on PPPs



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Discussion Paper

4 KEY ISSUES

- 1. Short and Medium term impacts of the crisis.**
- 2. Remedial Actions**
- 3. Adjustments**
Some grounds for optimism?
- 4. Impact on the model itself**
PPPs as a means for a 'sustainable' recovery?

Short – Medium Term Impacts of the Crisis

- **Fewer lenders in the PPP market**
 - Probably half the number and debt usually represents about 80% of the funding required for PPP transactions.
- **The amount any one bank is prepared to lend is 25-50% of what it was 2-3 years ago.**
- **Loan maturities are now much shorter**
 - With a reduction from 15-25 years or more, to 8-15 years now.
- **The cost (i.e. margins) for such loans has doubled or more**
 - Margins have increased from, say, 100 ‘basis points’ to 2-250 ‘basis points’ (or more!).

Furthermore...

- **Lenders prefer to:**
 - Lend to projects sponsored by existing clients/relationships, rather than new ones.
 - Lend to local markets.
- **Loans for more than 10 years** maturity puts the 'red light' up for any Credit Committee
 - So careful project structuring and presentation is essential.
- **Banks have spawned “PERMs”**
 - 8-10 year loans under which borrowers pay an increasing margin after years 7-8 to encourage re-financing (hopefully on cheaper terms).
- **Finally, has the leveraged Private Equity model seen its day?**

Remedial Actions by Governments

- Tried to keep PPPs afloat through **special measures**.
- Taken more **risk** to close deals.
- **Facilitating projects** where there is inadequate finance organizing competitions for finance amongst preferred bidders.
- **Offering guarantees** to the project's debt financiers.

Adjustments

Grounds for Optimism?

- **In transition economies - banks have withdrawn**
 - The lead will come from IFIs and the ECAs (e.g. in Kazakhstan the PPP financing option looks like PPP financing of 10 years ago!)
- **The question is:**
 - *Can these players – ECAs and IFIs respond effectively???*
- **Commitment of transition economies is still strong**
 - Everywhere a willingness to develop new techniques, new legislation and institutions.
- **One can review of the world market to date**
 - Shows that no project finance/PPP project has collapsed because of the crisis, although airports and ports have seen a 15-20% downturn in revenue.

Adjustments

Grounds for Optimism?

- Market adapting to the new environment
 - Highways in Poland and Florida - Deals are being closed, but at a slower pace.
- Banks are also returning to the market?
 - RBS re-opens project finance office?
- Even if there was no crisis, the PPP model is still highly complex and requires skills and knowledge that are in short supply
- Is it *lack of finance* or *lack of bankable projects*?
 - In turn lack of government capacity to generate bankable projects !

Impact of the Crisis on the PPP Model

- Crisis as an opportunity?
- Any signs of new PPP models emerging that will make the recovery a sustainable one?
- Lots of potential from the stimulus packages.
- Governments still need convincing on sustainability issues.
 - Has to be ones which make it cheaper to do PPPs that take into account green criteria.

Conclusions

- The crisis has had a negative effect on PPPs and made their development more difficult.
- Significant increase in the cost of debt for PPP projects.
- Substantially reduced maturities being offered by banks.
- Model is changing with a stronger public.
 - Greater guarantees, role of ECAs, IFIs and the model is adapting.
- Will it be a return to ‘business as usual’?
 - Will the banks come back?