WHY PSP IN TRANSPORT INFRASTRUCTURE MAY NOT BE SUITABLE TO DEVELOPING COUNTRIES

Rene S. SANTIAGO
CSM and Associates
Loyola Heights, QC, Philippines
Phone: +63-917-5386550
fax: +632-433-8181
e-mail: renesan@myway.com

Abstract:
In the 1990s, private sector participation (also known as PPP, BOT, or PFI) in the development and financing of transport infrastructure - like toll roads and urban rail transit system - was hailed as a boon to developing countries. After a decade of experience, the record of successful projects was very few. Controversies hounded the few that got into light of day.

This paper takes a critical look at the promise of PSP for developing countries in the region, by highlighting and comparing the problems and obstacles that hobbled a number of PSP projects during the last decade. Using the projects in the Philippines as a jumping board, the paper then briefly reviews the country-specific or project-related conditions that made so many of the projects fail, or a few to succeed. They raised a disturbing possibility: PPP may be the wrong tack for the Philippines, and perhaps raising false hopes also to many developing countries with similar factor conditions. The adverse conditions appear insurmountable: weak government institutions, absence of domestic long term capital markets, fundamental weakness of the transport market, and distorted expectations about PSP. The greater the shortcomings and the policy gap, the more likely these projects translate into financial time bombs.

The paper offers practical lessons to developing countries about the horrors and dangers of unbridled PFI in the pursuit of transport infrastructure.

Key Words: private sector participation, BOT, PPP, PFI

1. INTRODUCTION

1.1 The PSP Landscape

Since the 1990s, the private sector has become the new savior of infrastructure-hungry, but capital-strapped, developing countries. Private-financed infrastructure opened an alternative door to the conventional and well-worn path of project implementation. Many developing countries followed the siren call and scrambled to open their doors to private investors. An ADB-commissioned study (2000), however, found that “implementation experience has not matched expectations”. Looking at a handful of high-profile transport projects concluded in the region, one could not help but conclude that the handful could become a trickle, and the completed ones maybe ticking financial time bombs. Figure 1 shows the initial surge followed by a declining volume of investments in PFIs.
Annex 1 list recent expressway projects among Asian countries. It is also indicative of the (past?) popularity of BOT/PFI among Asian countries in the last decade, and the various stages these projects go through.

1.2 Terminologies

Transport projects have traditionally been implemented by the public sector, i.e. planned, financed, operated, maintained and owned by the government. To be sure, there were also various degrees of private sector participation – but not in the saddle seat nor in project finance. The magnitude of projects was limited only by what the public sector can raise via taxes and debts.

By the 1990s, implementation by the private sector emerged as a way of realizing projects, supposedly without increasing public sector liabilities. This non-traditional way came to be known under various labels, such as Build-Operate-Transfer (BOT), Private Financed Infrastructure (PFI), Public-Private-Partnership (PPP), Private Sector Participation (PSP), or Design-Build-Finance-Operate. Strictly speaking, PSP has a broader meaning as it includes privatization and management contracts with little or no private capital expenditure. On the other hand, PFI is more restrictive in that it entails major investments in new facilities (sometimes referred to as Greenfield project) with minimal support from the government. Under the umbrella of PFI, one may include Build-Operate-Transfer, Build-Lease-Transfer, Build-Own-Operate, Build-Rehabilitate-Operate-Transfer, and similar contracts. The ambit of PPP is a continuum from PSP to PFI, and generally implies (though not always) substantial government support. For purposes of this paper, these terms are used interchangeably, unless the context demands otherwise.

This paper also uses the term ‘developing, transition or emerging’ country (often, shortened into DTE) in a general sense, as referring to those countries characterized by low domestic savings rate, low per capita GDP, eligibility for ODAs, and inadequate transport infrastructure. Consequently, their needs are for Greenfield (and large) infrastructure projects – especially in their respective rural and poorer regions. Except for some state-owned enterprises, DTE countries have very little transport assets to privatize.

1.3 Transport Projects Are Unique

Infrastructure projects are not the usual stuff that private sector invests in. First, they entail large investments which can be recouped only over long periods of time. Once made, the assets can not be pulled out in the event of a downturn. Moreover, they carry a public character, hence, almost always politicized. They are therefore not the usual tradable goods. Europe (ECMT, 1989), despite its well-developed capital markets, has recognized the herculean efforts entailed in tapping private capital into transport infrastructure and accordingly, opted to scale down its PSP ambitions.
1.4 Basic Equation

Any PSP or BOT projects revolve around financial viability for the private investors and economic viability for the public sector. This is summarized in the following equation:

\[
ROI = \frac{S(\text{Net Income/Benefit}) \times Pr \pm S}{(\text{Cost}_1 + \text{Cost}_2)}
\]

where \(\text{Cost}_1\) = cost of project borne by private sector
\(\text{Cost}_2\) = cost of project assumed by public sector
\(S\) = support from the government either in terms of tax breaks, incentives, credit enhancement, subsidies, and the like.
\(Pr\) = probability of realizing the forecasted incomes

The objective of government is to get the project implemented with \(\text{Cost}_2 = 0\) and \(S = 0\). On the other hand, the objective of the private investor is to maximize ROI by minimizing \(\text{Cost}_1\) (which can only occur by increasing \(\text{Cost}_2\)), or increasing \(S\), or reducing risks (pushing \(Pr\) towards 1). The key to successful and sustainable PSP is to balance the two conflicting objectives.

1.5 Different Strokes for Different Modes

Are all transport modes the same? From a project financing viewpoint, and hence suitability to PSP, they are vastly different. Mahur, R. (2003) ranks airport terminal projects at the top of the heap - because of its natural monopoly elements and recourse to other sources of revenues. A similar tone came out of Silva’s (1999) analysis of 89 airport projects involving PSP in 23 DTE countries; airports have the unique combination of revenues denominated in foreign currency and operational costs largely in local currency.

Urban expressways are next in rank, especially when there is established high-volume traffic and the concession carries a non-competition clause. Mass transit projects should be the least attractive, largely because they are perennial money losers with very narrow revenue sources denominated in local currency. Toll roads and transit projects are both susceptible to network risk and depend on interconnections that are outside the control of project proponents.

The project structure tends to differ also among modes. In airports, the dominant pattern has been towards operation and management of assets with significant capital expenditures in existing assets. Most airport projects, according to Silva (1999) involved terminals and runway facilities, as well as terminals-only, with very few stand-alone runways. A similar O&M pattern and bias for terminals and cargo-handling equipment was observed for seaports (Sommer, 1999), where the PSP structure is built around the landlord model.

On the other hand, the “road sector is different from other infrastructure sectors because it is not commercial”, says the ADB report (2000).
2. BOT IN PHILIPPINES TRANSPORT

2.1 The Best (or the Worst)?

The Philippines was touted by the World Bank (Baietti, et.al., 2000) as having the best legal framework for BOT projects in the region. After a decade of actively pursuing PPIs in infrastructure, the Philippines could only show a handful of concluded projects – all of which were clouded by controversies, none can be considered a roaring success. The harvest: 1 in air transport, 1 in urban rail, 4 in toll roads (of which only 2 were completed). No port project has reached the first base, notwithstanding several attempts by port authorities to tap PSP since 1992.

Annex 2 shows the various transport projects from 1992 to 2002 that managed to reach the stage of concession agreements in the Philippines.

2.2 Airport Terminal 3 Project

The project to build a new terminal for Manila’s international airport began as a Presidential invitation to a group of businessmen (called Asia’s Emerging Dragons) in 1994. After spending time and money on studies, the ‘dragons’ was edged out – in a bitter process called ‘Swiss Challenge’ - by a joint venture between Frankfurt Airport Authority and a local air cargo handler. The award was made on the basis of highest rental payments (₱17.75 billion over the 25-year concession period), a criterion that would have been appropriate if the competing project designs and revenue assumptions were similar.

The project was a magnet for controversies – from start until now. Newspaper columnists of various shades took different sides. Legislative inquiries produced contradictory evaluations: the Lower House declared the concession contract as above board while the Upper House noted that the concession agreement was void from the start for failure to get the requisite approval of six members of the Cabinet-level Investment Coordination Committee (ICC), for deviating from the bid documents, and for contravention of the BOT law’s prohibition against direct government guarantees for projects arising from unsolicited proposals. By end November 2002, the President nullified the contract or more correctly, the series of contracts. The contract underwent four amendments – each time pushing the cost up and tilting the risk balance to the government side. By 2002, the construction bill was already US$657 million.

The creeping improvements in the position of the concessionaire, at the expense of the government, were later found to be onerous. Some of these were:

- Absence of ceiling on costs that can permit government regulators to set return-on-rate base, and consequently, determine charges for cargo handling, passenger terminal fees, aircraft parking and the like;
- It awarded a monopoly of land-side operations within Terminal-3, and replace existing sub-contractors at the old NAIA Terminal-1;
- The concessionaire got the freedom to decide rates on 12 of 16 revenue sources. The remaining 4 regulated fees were: aircraft parking and tacking, check-in counter and passenger terminal fees.
It raised terminal fee to an initial $20 (from $10) with provisions for future increases. Comparative figures are: $7.20 in Indonesia, $8.60 in Taiwan, $9 in Singapore, $10.30 in Hong Kong, $11 in Malaysia and Thailand, and $11.50 in Vietnam.

The revised contract required government to issue loan and other guarantees, in case the concessionaire defaults on payments to lenders.

It assigned insurance policies solely to the project’s "senior lenders."

Asymmetrical assignment of contingent risk, with the government obligated to pay the concessionaire higher liquidated damages than if it was the other way around.

Performance testing was dropped as a pre-requisite to the issuance of a Certificate of Project Completion.

A tunnel linking Terminal 3 to Terminal 2 (at a cost of P800 million) was removed from the concessionaire’s obligations, and replaced by an access road to be shouldered by government.

Airport projects under PSP are supposed to be prosaic. As it turned out, the Terminal 3 Project became a microcosm on what can go wrong in PSP – particularly in the Philippines. The erstwhile joint-venture partners quarreled among themselves as cost ballooned against a background of disproportionate allocation of the gains and pains during construction. The contract underwent revisions from one government administration to another, each time tilting the balance against public interest, made possible by rent-seekers.

Contrary to economic theory, the concessionaire had the incentive to jack up construction cost – as it created opportunities for frontloading profits with only too-willing a government consenting to their eventual recoveries from the public. Government regulators had the same incentive because the bid-award criterion meant a bigger share of future incomes (no matter how mythical).

Investors expect stability and enforceability of contracts. Thus, it would be unfair to private investors when a new government takes over and reverses decisions of the previous ones. In this case, however, it was not completely innocent as it invited reversals when it sought contract amendments. On the other hand, it is also unfair when egregious terms won after (not during) the bidding are left untouched. What this proves is that PSP contracts can only be stable if founded on fairness and equity.

2.3 Toll Roads Projects

If the sheer number of proposals was the gauge, toll roads in the Philippines are extremely attractive investments. A recent study (Almec, 2002) for JICA counted 18 expressways that were mooted during the past decade – 4 of which managed to get into contract signing, but only 3 achieved construction.

The Skyway and the Manila North Tollway projects are particularly noteworthy. Folded into both projects were established, albeit aging, toll roads with robust traffic and growing revenue streams. They were, therefore, less risky than Greenfield projects. Phase 1 of the former opened in 2000, and phase 2 was supposed to commence immediately thereafter. It has not. Less than forecast traffic on the expensive elevated segments, compounded by short-term foreign-denominated loans against local currency incomes, and the Asian-wide contraction of funding supply, have caused a financial hemorrhage. Lenders are now wary to extend more credits for Phase 2. But without extension, traffic on the elevated toll road would remain sluggish. It is, therefore, now in a classic catch-22 bind.
There is another negative, but less obvious to non-transport experts, long-term impact of the Skyway project: it had considerably reduced options for upgrading the south commuter rail line, a mass transit-oriented solution that offers higher-capacity on the corridor at much less cost. A broader strategic evaluation could have prevented this from happening.

In comparison, the Manila North Tollway failed to start construction before 2003 despite its better credentials: pedigreed sponsors and lenders (which counted ADB and IFC), less-expensive at-grade solutions, and support of top officials. If a project of this kind can encounter much turbulence, what chances can other PSP projects of lesser-viability have?

As can be gleaned from figure 2, the various toll road projects under consideration exhibit varying viability. Those showing financial returns lower than 15% are unlikely to secure financial backing – without substantial government support. And yet, authorities and proponents of these potential money-losers keep stoking their PSP fires. All the while, charges on the existing North and South Luzon Expressways were kept stagnant for about 17 years, a flawed policy that prevented their improvements in the first place and paved the way for the subsequent Skyway and Manila North projects.

![Figure 2 – Comparative Returns on Several Proposed Toll Roads in Philippines](source: Almec (2002), Development of PPP Technique of Manila Urban Expressway Network)

2.4 Fascination with Rail

Manila’s LRT 3 could claim to be the first to be signed (in 1991, though not the first to be completed) rail project under the PFI/BOT umbrella in the Asian region. Its proponents, as well as the government, touted it as the first urban rail project in the world to be financially viable. The facts, however, were the opposite. In 2001 and 2002, the Philippine government had to scrape the bottom of its budget to extend $60 million a year in subsidy.

Predating the Terminal 3 project, the concession agreement for LRT 3 underwent eight amendments – raising the project cost from $350m to $675m. As if one mistake is not enough, a 5-km extension is being promoted as the financial savior that will turn around
billions of losses into profits for the government. Inspired by its ‘success’, a former high-
government official - who should know better - has turned into a sponsor for yet another 
rail project that did not even exist before in many previous transport studies on Manila.

A surprising high number of urban and rural railway projects requiring more than $9.7 bil-
lion (Santiago, 2001) are being dangled for PSP implementation in the Philippines. Noth-
ing in their designs would suggest that they could ever become exceptions to the well-
known weaknesses of rail systems. And yet, news about their impending constructions 
keep on popping out for the last 5 years, endorsed by a President promising to triple Ma-
nila’s rail network in 6 years through private investments!

3. PSP IN OTHER COUNTRIES: DIFFERENT BUT SIMILAR

3.1 A Tale of Mass Transits in Three Cities

Nothing illustrate the paradox of PSP better than the fortunes of seven high-profile urban 
rail projects that were launched in the cities of Bangkok (the Green, Red, and Blue Lines), 
Manila (the LRT 3 and LRT 1 Extension), and Kuala Lumpur (STAR 1 and Putra LRT2). 
A brief comparison of these PSP projects is shown on Table 1. These projects had differ-
ent project structure and risk allocations - 4 were completed, 2 aborted, and 1 on the fin-
ishing stages of construction. All shared the fate of urban rail systems around the world – 
of being money losers.

The uncompleted ones are the Red Line (aka Hopewell’s BERTS) in Bangkok, and the 
LRT 1 Extension in Manila. The former was structured as a BOT, while the latter was 
structured as a joint venture with government assuming the cost of the civil works and the 
private proponent providing the electromechanical components. In short, a greater share of 
the risks was assumed by the Philippine government than that of Thailand; yet, both pro-
jects failed to take off. Despite its bigger risk burden for the private proponent, BERTS at 
least managed to break grounds and build a few columns. In contrast, LRT 1 Extension 
has not gone beyond contract signing. With a similar joint-venture structure, Bangkok’s 
Blue Line is nearing completion and posed to open in August 2004.

With higher private risk allocations than those in Bangkok and Manila, the two rail pro-
jects in Kuala Lumpur secured financing quickly and became operational in 1998. Not 
unexpectedly, they incurred financial losses since start of commercial services. The Malay-
sian government subsequently bailed out the proponents. The Green Line of Bangkok, 
which became operational in December 1999, also suffered tremendous losses. It is cur-
rently able to service only 25% of its daily interest charges [Wai-mun, 2003], and is now 
in the midst of painful (to lenders and investors) financial re-structuring.

Of the 7 projects, the MRT 3 of Manila had the most lopsided risk allocation profile 
against the government, but took the longest to get financial closure. Aside from assuming 
traffic risk, the Philippine government extended loan guarantees and provided the lands for 
the right-of-way, depot and commercial developments. It also consented to 8 revisions to 
the concession agreements, pushing the costs up by 193% from its original price.

Despite experiences to the contrary, five of the rail projects promised financial viability 
which their sponsors, lenders and host governments believed (or pretended to believe).
These were: Manila’s MRT3, Bangkok’s Green and Red lines, and Kuala Lumpur’s LRT 1 and LRT 2 system. Was this a case of self-delusion? Estache(2000) attributed this kind of behavior to the exuberant lending before the Asian crisis of 1997 as well as over-optimistic proponents who relied on heavy debt financing for heavy-risk projects, and short-term loans for long-term projects. The unseen hand of mercantile interests from developed countries is rarely mentioned, but could account for the steam behind rail projects.

Table 1. Comparative Data of Seven PSP Rail Projects in Three Asian Cities

<table>
<thead>
<tr>
<th>CITY</th>
<th>PROJECTS</th>
<th>COST ($)</th>
<th>PSP MODEL</th>
<th>REMARKS</th>
</tr>
</thead>
<tbody>
<tr>
<td>MANILA</td>
<td>LRT3 – Edsa Line</td>
<td>$675.5 m</td>
<td>Build-Lease-Transfer</td>
<td>Partially opened in 12/99; full line in 2000. Failed to live up to its</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(17.8km, 13 stations, mostly EL)</td>
<td>25-year concession; State to operate. Market risk &amp; loan guarantee by State</td>
<td>claim of no State subsidy</td>
</tr>
<tr>
<td></td>
<td>LRT1 – South Extension to Bacoor</td>
<td>$597m</td>
<td>JV with LRTA; Civil Works as gov’t liability but EM system by private; existing line folded into the deal</td>
<td>Failed to meet target construction start by 4Q2002. Revenue sharing according to value of contribution</td>
</tr>
<tr>
<td></td>
<td>BERTS (Red Line)</td>
<td>$2,200m</td>
<td>BOT on 30-year term. Hopewell was to pay Baht600m/yr in fees, even before start of operation</td>
<td>Aborted in 1998. Columns and other structures to be demolished</td>
</tr>
<tr>
<td>BANGKOK</td>
<td>Skytrain (Green Line)</td>
<td>$1,200m</td>
<td>Build-Own-Operate-Transfer (BOOT) 30 years concession</td>
<td>Opened in Dec 1999 Concessionaire in dire financial re-structuring talks.</td>
</tr>
<tr>
<td></td>
<td>Metro (Blue Line)</td>
<td>$2,500m</td>
<td>State (MRTA) taps ODA for civil works; BOT for E&amp;M system</td>
<td>To open in 2004 Concessionaire pays MRTA</td>
</tr>
<tr>
<td>KUALA LUMPUR</td>
<td>Star 1</td>
<td>$120 m (Ph1) + $765 m (Ph.2)</td>
<td>BOO 30 years + 30 years State provide ROW</td>
<td>Ph.1 opened in 1996; Ph. 2 opened in 1998. Defaulted on loans, rescued by government</td>
</tr>
<tr>
<td></td>
<td>Putra 1</td>
<td>$1,200m</td>
<td>BOO 30 years + 30 years State provide ROW</td>
<td>Section 1 opened in 1998; full line in 1999. Defaulted on loans, rescued by gov’t</td>
</tr>
</tbody>
</table>

3.2 Government is Only One Side of the PSP Coin

One of the lessons being drummed to entice more PFIs is for governments to improve their processes, reform their policies, re-design or strengthen their regulatory institutions. The premise is that the reforms would bring in the hordes of investors, assured by an impartial, independent, and knowledgeable regulatory unit. The Philippines, and other Asian countries, have – in varying degrees – adjusted their processes to the tune of PSP music.

And yet, as is apparent in the aforementioned 7 similar rail projects in different cities, the same ‘music’ produced different results. The government is only one side of the PSP coin, the other is the private sector.
Even if countries could reform their processes overnight, and their governance become a model of market-friendly institutions, a deluge of investments into transport infrastructure may not materialize. PSP is sensitive to many conditions beyond the control of individual countries. It takes two parties - an investor willing to take risk and a hospitable government - to realize a PSP project. So a government can bend backwards as much as it can, but not produce any change in the investment climate. The Asian financial crises of 1997 and sovereign defaults in other regions of the world have reduced considerably the appetite for PSP projects.

And yet, government is almost always cast as the villain for project failure. "While the BOT Law rationalizes private sector participation in infrastructure provision, it provides very limited protection for the investment of the proponents" (Batac-Antonio, 2002).

3.3 A Journey of a Thousand Miles

PSP is not a walk in the park. Experiences from many countries have shown that the ride is not only rough, but may also be a roller-coaster journey. To succeed, the government had to do more, aside from delivering specific project support. Up to what extent DTEs can prostrate themselves is a big question.

Estache (2001) pointed to the poor quality of project preparation for the failure of most of the 52 road concessions for 5,550-kms of roads awarded by Mexico from 1989 to 1995. The ADB (2000) echoed the need to prepare the legal, regulatory, and contractual environment first before embarking on a PSP journey. The groundwork is only a prelude to a lengthy process – prescribing selection of projects in the context of an overall transport strategy, followed by rigorous project preparation, a transparent bidding process, contract negotiation, delivery of government support, and enforcement of the concession agreements. It is a very demanding process for which bureaucracies in developing countries are not accustomed to handle. Training of personnel has been proposed as a solution, but it is doubtful whether the expertise will ever be nurtured in a governmental organizational culture.

Lack of understanding about private sector motivations, as well as ill-suited governmental procedures, meant that the approval process for BOT projects often span several years. In the Philippines, a government study found out that the half-life of the procedural hurdle is about 3 years, with possible improvement to a barest minimum of 416 days.

Lenders specializing on project finance view the ensuing transactions as more complex than traditional corporate or public financing, resulting in significantly higher transaction costs to the tune of 7-10% of total project cost and twice as much as straight debt or equity finance. The same complexity is often used as an excuse to mask shady deals.

PSP is a long, tortuous, and expensive journey to a destination that may turn out to be no better than the old route.
4. GENERIC ASPECTS OF PSP

4.1 Paradox of Project Finance

Regardless of countries and modal differences, PSP requires long-term financing. DTEs. Cash outflows are heavy during the early years, and positive cash generations come in only at the mature stage of the infrastructure. In figure 3, Dailami (1997) pointed out that the risk differentials for a theoretical project costing $1,000 could reach as much as 50% between two loans of 15-year and 5-year maturities. Usually, long-term money is not available domestically in DTE countries, hence the recourse to international funding sources.

Another facet to the funding issue is that the money is not yet in the bag at the time of award of the concession. Theoretically, the financing plan is part of the reason for award. It could not, however, be secured without the award. When the project loan is subsequently negotiated, lender-driven covenants usually arise that require contract revisions, and of course, alter the risk-sharing equation. Irwin, et.al. (1999) suggest that government do not assume risks outside its control, but because of the project’s momentum after contract signing, the government tendency is to capitulate and bear the additional risks. A weak project sponsor compounds the problem, by inviting more stringent lender conditions that ultimately ripple back to government.

Parameter assumptions are: i) Initial investment = $1000, financed with a mix of $200 equity and $800, debt; ii) Loan payment = end-of-period equal amount; iii) Rate of return on the project = 25%; iv) Distribution of project revenues, net of all non-capital production expenses, assumed to be normal with mean = 250 and with standard deviation that is assumed to vary from 12.5 to 250 with an increment of 12.5; and v) Debt service ratio = 1.1.

Figure 3 – Project Risk and Loan Maturity
4.2 In Search of Marathoners

PSP requires a long-term view. Both parties to the agreement should be marathon runners, and not sprinters.

Because of this element, the concession agreement tries to anticipate all possibilities in the future – something no one has the infallibility to predict. This gives rise to complex interlinking of conditions – many of which have yet to occur. The private parties – if concerned with long run profits – will (and can) protect itself against all possible scenarios. If ‘sprinters’, it could siphon off profits during construction and could not care less what happens afterwards.

It is the government side that is worrisome: the parties signing on its behalf are ‘sprinters’ who will no longer be around to answer when the going gets rough. They can claim the credit, but it is the future generations that end up paying for their mistakes (and misdeeds).

4.3 Looking After Public Interest

This brings us to the question on who protects the public interest in PFI deals? An independent regulator is often recommended as an imperfect solution, but it maybe an oxymoron. When the regulator is vulnerable to capture by the regulatee, and the government itself is beholden to business interests, such an expectation becomes unrealistic. Neri (2002), using Hutchcroft’s matrix (see table 2), classified the Philippines as an oligarchic state where business influences the state to benefit its self-interests. Therefore, a PSP program for States under categories III and IV would naturally converge into lopsided deals.

Table 2 - Classification of Countries

<table>
<thead>
<tr>
<th>Rational/Legal States</th>
<th>State &gt; Business (Strong States)</th>
<th>Business &gt; State (Weak States)</th>
</tr>
</thead>
<tbody>
<tr>
<td>II – Developmental State</td>
<td>State establishes policy to create an environment for progress and wealth, like Singapore</td>
<td>I – Laissez Faire Regulatory State</td>
</tr>
<tr>
<td>Business pursues wealth while State watches over public interest, like USA</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Predatory States</td>
<td>III – Bureaucratic Capitalism State dictates who in business controls wealth, like Suharto’s Indonesia</td>
<td>IV – Oligarchic State (Booty Capitalism)</td>
</tr>
<tr>
<td>Business influences state policy to benefit its self-interest, like the Philippines</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Romulo Neri, Asian Institute of Management, as reported in Philippine Star, 13 March 2002

The above table also helps explain why the various PSP projects in the Philippines became objects of controversies. And why similar projects, like the 7 rail projects in Table 1 that tapped into the same project finance markets, yielded different risk balances.

Not unlike the radical public sector reforms adopted by New Zealand (Schick, 1998), PSP may not be appropriate to many developing countries.
5. CONCLUSIONS

Expectations of a deluge of investors competing for concessions - at no cost to the public sector - have not happened. On this yardstick, looking for that successful transport project is like looking for the proverbial needle in a haystack.

As the ADB (2000) study found out “not all countries are suited to PSP, particularly to major BOT projects.” And because of the experiences of the past decade, project financing institutions have virtually closed the door to some DTEs or insist on extended risk premiums that could virtually raise the cost of capital, according to Estache, et.al. (2000) estimates, by more than 5% and thereby push the project into non-viability.

Without necessarily recommending a complete abandonment of PSP, this paper contends that developing countries should avoid hitching their wagons to the PSP horse. The horse may never come, for a number of reasons: (a) poor or inchoate domestic capital markets which in turn forces a reliance on foreign capital; (b) foreign investors and lenders that had turned picky and jittery, (c) complex deals that exact heavier workloads on government institutions than traditional mode of project development, (d) low affordability of transport users, (e) politically-determined decisions that prevent cost-covering tariffs, (f) weak or poorly structured regulatory institutions that are either anti-market or vulnerable to capture by parties to be regulated, (g) concession periods that need to be long for capital recovery but has to navigate changes in political leadership and policy discontinuities, (h) general inability to deliver the requisite scale and phasing of government support.

REFERENCES


APPENDICES

Annex 1: Asian PSP Experience-to-Date in Expressway Projects

<table>
<thead>
<tr>
<th>Country</th>
<th>Open</th>
<th>Construction</th>
<th>Planning</th>
<th>Pre-Planning</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bangladesh</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
<td>5</td>
</tr>
<tr>
<td>India</td>
<td>11</td>
<td>4</td>
<td></td>
<td></td>
<td>15</td>
</tr>
<tr>
<td>Indonesia</td>
<td>2</td>
<td>6</td>
<td>7</td>
<td>20</td>
<td>35</td>
</tr>
<tr>
<td>Laos</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Malaysia</td>
<td>12</td>
<td>7</td>
<td>13</td>
<td>8</td>
<td>40</td>
</tr>
<tr>
<td>Pakistan</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td>4</td>
</tr>
<tr>
<td>Philippines</td>
<td>3</td>
<td>1</td>
<td>10</td>
<td>1</td>
<td>15</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Thailand</td>
<td>7</td>
<td>3</td>
<td>2</td>
<td>1</td>
<td>13</td>
</tr>
<tr>
<td>Vietnam</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>TOTAL</td>
<td>29</td>
<td>17</td>
<td>49</td>
<td>38</td>
<td>135</td>
</tr>
</tbody>
</table>


Annex 2 – Philippine Transport Projects with Private Sector Financing

<table>
<thead>
<tr>
<th>Name of Project</th>
<th>Description</th>
<th>Key Dates</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>MRT-3 (urban rail)</td>
<td>Structured as a Build-Lease-Transfer scheme, where government is the operator.</td>
<td>First signed in Nov 1991 with a project cost = $350m; Construction started in Oct 1996; Contract underwent 8 revisions and pushed cost to $675.5m; Full-line commercial operation by June 2002</td>
<td>Completed beyond original promised date (of 1995) and cost. Promised no subsidy, but incurred $60m subsidy in 2002. Foreign loan guaranteed by government, which was not in original deal. Traffic below forecast.</td>
</tr>
<tr>
<td>LRT 1 South Extension</td>
<td>A joint venture between a foreign entity and SOE, on BOT scheme</td>
<td>Joint-Venture Agreement signed by SNC Lavalin in Sept 2000; Financial closure supposed to happen by 4thQ2002.</td>
<td>Supposed to start construction by 4Qtr2001, and be in commercial service by May 2004. Currently stalled. Gov’t undertaking not permissible to projects that did not go through open tender.</td>
</tr>
<tr>
<td>Star Project (toll road)</td>
<td>42-km of 4-lane divided expressway to be built in</td>
<td>Concession Agreement was signed on 18 June 1998.</td>
<td>Private-financed portion is stalled, as proponent is unable</td>
</tr>
</tbody>
</table>

Concessionaire chosen from lowest-toll fee to be charged under a BTO structure. 2 stages. Stage 1 was funded by government using ODA, while stage 2 (cost= $) is to be funded by concessionaire. Target date for opening was January 2000. to secure financial closure. It has advanced ~$10m for rights-of-way, which was supposed to be a government undertaking and support.

<table>
<thead>
<tr>
<th>Manila North Tollway (toll road)</th>
<th>Rehabilitation of 82-km existing tollway, plus 2 new lanes x41.2km. New section involves 81.4km to Subic and C-5 road within MM Manila. Cost= $371m</th>
<th>Concession agreement signed June 1998. Construction period from 1996 to 2002. 8.5km Subic-Tipo section was advanced and completed in 1996. But 8 other stages delayed due to rights-of-way problem. Lenders withheld fund releases until conditionality are met.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Recruitment with existing franchise holder, on BTO scheme</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manila-Cavite Toll Expressway (toll road)</td>
<td>At-grade 25.2km to be developed in 3 phases. Phase 1 involved upgrading to 6 lanes of an existing 6.45km road. Phase 1 cost ~$21m.</td>
<td>First toll concession awarded in May 1990 to PEA, an SOE. In Dec 1994, PEA entered into a joint venture agreement with MARA and Renong group of Malaysia. Construction began in Nov 1996. Toll collection started in May 1998. Phase 1 was completed in May 1998. Proponent advanced $68m for rights-of-way acquisition for Phase 2, which remained uncompleted.</td>
</tr>
<tr>
<td>Joint-venture between a foreign firm and SOE (PEA), using a BTO structure</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NAIA 3 Terminal (airport)</td>
<td>Intended to be the new international airport terminal capable of handling 10m pax/year, with 31 aircraft stands and 190,000 sqm floor area. Original project cost = $350m.</td>
<td>In 1994, President invited a group of businessmen to develop the terminal. Concession agreement signed in April 1997. Construction began in June 2000. RP President announced in Nov 2002 the nullification of contract. Original contract got amended 4x, which raised the cost to $657m and secured government loan guarantee. Foreign partner, Fraport, wants out. Failed to open in Dec 2002, due to several defects.</td>
</tr>
<tr>
<td>BOT structure, awarded after 'Swiss challenge' on basis of highest payment to government.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: Information culled by the author from several published and unpublished sources, as well as personal knowledge.*