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PPPs in transport

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Introduction

- Private finance for public infrastructure - rationale and mechanisms
- Financial outcomes
  - Evidence about the additional cost of private finance
  - Winners and losers
  - Role of financial advisors
- Conclusions
  - Expensive
  - Redistribution not value for money or risk transfer
  - Creates additional risks and liabilities
  - More than half by capital value have collapsed/required bailout

Public Private Partnerships (PPP)

- Private finance initiative (PFI) and design build finance and operate (DBFO) – long term contracts for the extension and maintenance of existing roads
- Partnership -joint ventures/part ownership, eg National Air Traffic Services
- Stand alone projects with user charges eg toll roads, bridges and tunnels for new crossings/roads, possibly with some public support
- Concessions, leasing and franchises, eg national railways, light rail (with subsidies)

Rationale

- >> More investment
  - Access private finance for investment
  - Not dependent upon gov debt + fiscal rules
- >> Value for money
  - Freedom from gov interference
  - Greater private sector efficiency
  - Competition
  - Risk transfer
- >> greater efficiency and economy from which all will benefit

Financial evidence from:

- Roads (Shadow tolls, Spain, M6 Toll Rd, M25)
- London Underground PPPs
- National railways
- Air traffic control
- CTRL

Shadow toll roads

- Existing roads
- Known as DBFO contracts
- Some new construction, ops and maintenance, shadow tolls
- Shadow tolls or availability payment where gov pays on behalf of users
- Viewed as success
- Little clear or detailed financial information
- Little political visibility
- Relatively straightforward/maintenance successful due to engineering standards

First 8 DBFOs

- First 8 schemes:
  - Annual cost about £220m
  - £6bn over 30 years
  - Paid £618m in 3 years
  - Construction costs were £590m
- Highways Agency said that paying 20% budget for 8% network
- An additional scheme means 40% budget for about 12-15% network
- Affordability - Impact on other roads?

Private sector accounts: cost of financing roads via private finance

(£ms)	A74M	UK A55	RMS A13	8 DBFOs	M6 Toll	Spanish Toll Rds (Euros m)
Year ending	June 2004	March 2005	Dec 2005	2004	June 2006	2003
Income (£m)	22	14	25	176	51	1,428
Expenses/income	23%	36%	36%	41%	53%	43%
Interest payable/income	59%	57%	62%	47%	88%	17%
Tax payable/income	4%	2%	4% rebate	6%	0%	19%
Post tax profit/income	14%	7%	4%	37% Affected by other income	loss	38%
Finance/income from state or user	73%	64%	68%	82%	88%	55%

Additional cost of private finance to state or user

(£m)	A74M/M	UK A55	RMS A13	8 DBFOs	M6 private toll road	Spanish Toll Rds Euros (m)
Year ending	**2004**	**2005**	**2005**	**2004**	**2006**	**2003**
Actual cost of debt	9%	7%	7%	9%	6%	6%
Interest payable on debt	13	8	16	82	45	238
Post tax profit	3	1	1	63*	-21	546
Total returns to providers of finance	16	9	17	145*	45	784
Interest payable at public sector rate	7.75% 12	4.75% 5	5.6% 13	8.0% 74	4.9% 41	7% 288
Extra cost of private finance	**4**	**4**	**74**	**71***	**4**	**496**
Extra cost of private finance as % income	**18%**	**29%**	**16%**	**40***	**8%**	**35%**

M6 toll road

- New 22m motorway
- Original strategic case not in public domain
- Direct tolls
- 54 year concession
- Loss maker due to low traffic volumes
- Refinancing deal
- To build a new toll free motorway on refinancing proceeds at no charge to gov to increase traffic
- Denied information via Freedom of Information requests
- Broader transport objectives and strategy?
- Who determines transport policy?
- Unsolicited proposals
- M25 widening

London Underground PPPs

- Three contracts to maintain and upgrade LU
- Extra cost of private finance >> £1bn a year subsidies (x 5 previous amount)
- DfT guaranteed private sector debt – banks did not pass on saving
- Gov provided TfL with letters of support if/when things go wrong
- 2 contracts late and over £2bn budget
  - Arbiter refused to allow them to recoup from LU
  - Went into administration
  - TfL had to pay their debts
  - Contracts taken back in house and investment scaled back
  - 3rd PPP terminated at break point

London Underground PPP

	London Underground PPP Tubelines	London Underground PPP Metronet BCV	London Underground PPP Metronet SSL
Year	2006	2006	2006
Income (£m)	927	342	320
Outsourcing as % income	66%	45%	49%
Operating expenses as % income	79%	86%	89%
Interest payable as % income	11%	9%	6%
Tax payable as % income	2%	0%	1%
Post tax profit as % income	5%	4%	3%
Finance (interest and post tax profit) as % income	16%	13%	9%
Finance and leakages via subcontracting (assumed to be 10% cost) as % income	**£194m** **21%**	**£61m** **17%**	**£47m** **15%**

National Railways

- Broken up into 100 companies and privatised a loss making but economical railway
- Train operators have franchise to run services – PPP
  - Lease trains – fully paid for in 7years, 30 year life
  - Pay to use track
  - Huge additional subsidies to TOCs
  - Loss makers without subsidies
  - Franchises renegotiated + subsidies increased
- Subsidies/grants to infrastructure operator
- Nearly 50% subsidies due to returns to providers of finance – double that before privatisation in both absolute and relative terms

Cost of new trains under public debt v cost of leasing trains from Roscos in UK

(£m)	**Annual finance charge**	**Total finance charge**	**Maintenance cost for 30 years**	**Total cost over 30 years**
7 year loan	687	4,800	2,500	7,300
10 year loan	513	5,100	2,500	7,600
20 year loan	315	6,300	2,500	8,500
25 year loan	277	6,925	2,500	9,425
30 year loan	253	7,590	2,500	10,090
Leasing for 30 years including maintenance	287			8,610

Financing costs in the UK's privatised railways

(£m)	British Rail 1994	1997	1998	1999	2000	2001	2002	2003
Total income	3,645	5,075	5,347	5,381	5,376	5,695	6,769	7,417
Train operators leakages		67	216	158	184	56	220	207
Leasing Companies' leakages		382	416	308	381	326	302	306
Network operator's leakages		238	218	272	407	448	*Not available	528
Freight Cos' leakages			21	17	7	8	37	20
Total leakages	121	794	871	755	979	838	559	1061
Subsidies	545	2,115	1,858	1,615	1,441	1,250	1,698	2,263
Leakages as % income	3%	16%	16%	14%	18%	15%	8%*	14%
Leakages as % subsidies	22%	38%	47%	47%	68%	67%	33%*	47%

National Air Traffic Services PPP

- Joint venture
- Sold 51% shares to consortium
- Loaded NATS with debt
- Unviable – based on rosy scenario
- Government bailout after 3 months
- Can't be allowed to fail
- Risks borne by state

Role of financial advisors

- Evolution and direction of policies determined by financial advisors
- Formulation of policy advice to govt driven by private sector staff on secondment or loan
- Project advice to both public and private sector
- Revolving doors, lobbying, sponsoring research
- Carry out implementation
- Carry out evaluative studies of PPP policy
- Advocate switch to market-orientated, not needs based, approach

Change in cost structure of UK public expenditure 1977-1996

	1977		1986		1996	
(£m)	Purchase of goods and services	Wages costs	Purchases of goods and services	Wages costs	Purchases of goods and services	Wages costs
General gov expenditure + social services (Excluding benefits and debt servicing)	5,571	14,209	17,488	34,680	49,360	67,411
As % operating costs	28%	72%	34%	66%	42%	58%

Change in cost structure of UK public expenditure 1997-2005

General government expenditure, less welfare payments, capital expenditure and health

	1997	1998	1999	2000	2001	2002	2003	2004	2005
Wages as % operating costs	55%	54%	52%	53%	53%	54%	52%	52%	51%
Other expenditure as % operating costs	45%	46%	48%	47%	47%	46%	48%	48%	49%

New sectors and companies

- Via commodification or creation of new services
    - Road tolling
    - Road pricing dressed up as congestion charging/greenery?
    - Train leasing companies
    - Train operating companies
    - Maintenance companies
    - Air traffic control
- Created new corporations, some of largest on LSE
- Increasingly taken over and incorporated into transnational corporations
- Non-traded services have been integrated into the international economy

Financial outcomes

- Workforce – jobs, wages and conditions to make way for dividends
- Price rises to cover additional cost + investment
- Skimped on investment (rail)
- Fragmentation >> loss of planning and coordination
- Takeovers – at inflated prices, paid for via debt which target company has to pay for
- >>Private monopolies
- Increasingly debt laden – financial sector benefits

Conclusions

- While the gov claims the policy is a success, the outcomes do not match the claims
- Winners = financiers, losers = taxpayers, workforce and users
- Risk transfer/additionality = legitimising rationale
- Creates additional risk – spreads risk
- Risks v rewards
- Hand back the keys+debt when things go wrong
- Can walk away from trouble
- Confirms the international experience