



PPP developments in the United Kingdom - an evaluator's view

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Three topics of common interest:

- Recent commentary on PPP profits and rates of return
- Improving ex-ante and ex-post project evaluation
- Challenges to the value for money of PPP projects arising from the banking crisis

Extensive public and parliamentary commentary on the cost of PPP

Popular and Trade Media

- Widespread perception of ‘super profits’ for investors in ‘low risk’ projects

Treasury Select Committee 19:viii:2011

- No convincing evidence that savings and efficiencies during the lifetime of PFI projects offset the significantly higher cost of finance. The average cost of capital for a low risk PFI project is over 8%

Public Accounts Committee 1:ix:2011

- The UK has 700 PFI contracts delivering a wide array of public assets and services with 61 further contracts under active consideration. Restrictions on capital budgets have meant that many of the assets delivered by PFI, including hospitals, schools, prisons, courts and roads might not otherwise have been built
- The committee suspects that initial investors are able to make excessive profits from selling PFI shares, yet lacks the information to know for sure

'EX-ANTE' EVALUATION MATRIX (1)

| | Strategic analysis | Tendering | Contract completion |
|---|---|---|---|
| Fit with business needs | Outline Business Case with clear deliverables | (2) Robust output specification | (3=) Clear cut contract Final Business Case |
| Appropriate delivery mechanism | Results of options analysis allowing for Optimism Bias | Baseline of service performance | Review of evaluation – did the market deliver as expected / required |
| Stakeholder support | Review of consultation | Review of stakeholder buy in | Key stakeholder support |
| Quality of project management | Design of project management | Effective team respect timetable | Contract management arrangement |
| Balance of cost, quality and finance | (1) Affordable based on market soundings | Good quality compliant and bankable bids received | Analysis of costs and the financing terms for debt & equity |
| Quality of risk management | Analysis of scope for risk transfer | Risk management procedures | (3=) “Appropriate” risk transfer agreed |

'EX-ANTE' EVALUATION MATRIX (2)

| | |
|---|--|
| | Strategic analysis |
| Fit with business needs | Outline Business Case with clear deliverables |
| Appropriate delivery mechanism | Results of options analysis allowing for Optimism Bias |
| Balance of cost, quality and finance | Affordable based on market soundings |
| Quality of risk management | Analysis of scope for risk transfer |

Optimism Bias

1. UK Treasury introduced the concept of optimism bias (Flyvberg et al) into its guidance on appraisal and evaluation in 2003
2. Authorities should use generic data or develop own historical sector specific data

Weakness

Typically applied to public sector costs, but often not to the likelihood of private sector delivering assumed benefits (in full)

'EX-POST' EVALUATION MATRIX

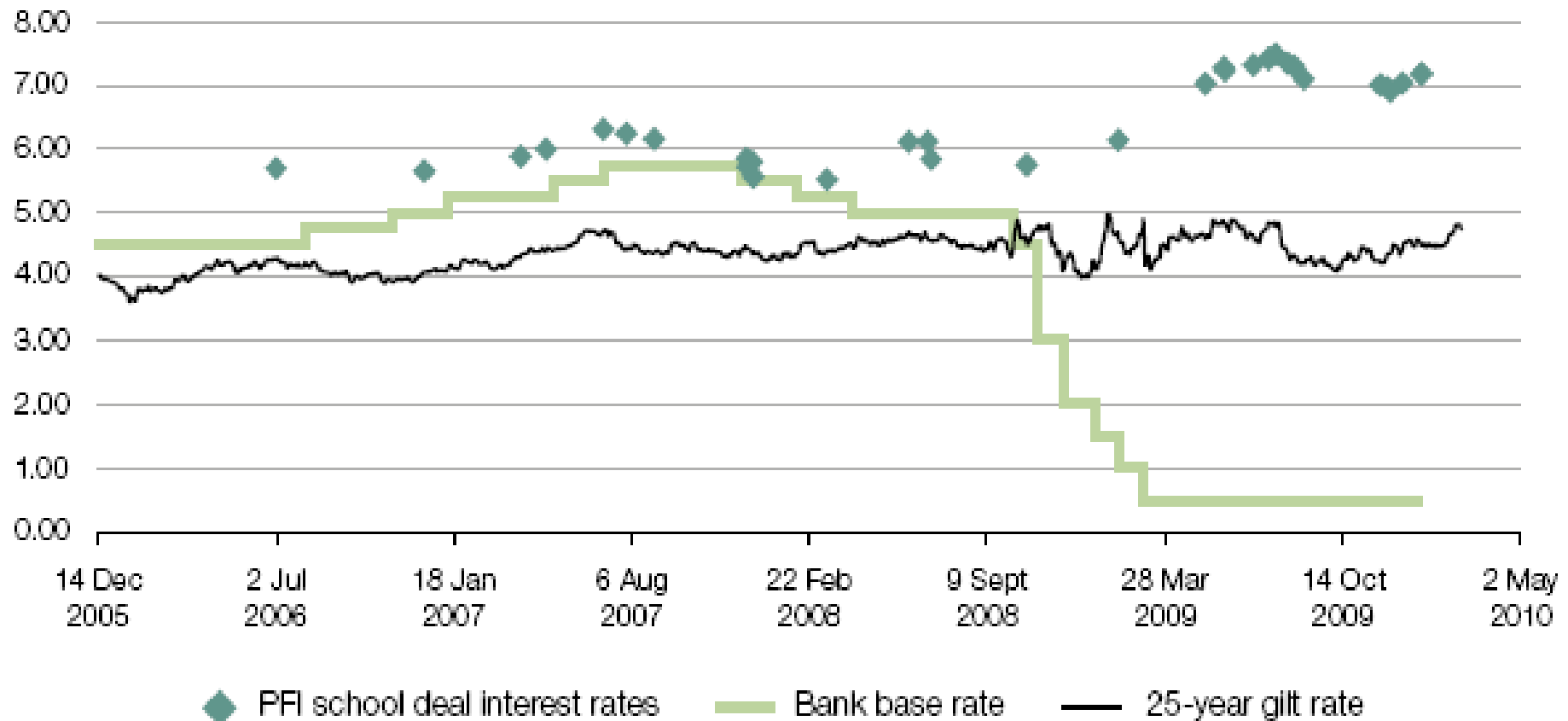
| | Strategic analysis | Tendering | Contract completion | Asset construction | Early operational | Mature operational |
|---|---|---|--|-----------------------------------|--|---|
| Fit with business needs | Good business case with clear deliverables | Robust output specification | Clear cut contract | Delivery to specification | Contract being met | Service meeting requirement |
| Appropriate delivery mechanism | Results of options analysis | Baseline of service performance | Review of evaluation | Delivery to specification | Review of performance | Review of performance |
| Stakeholder support | Review of consultation | Review of stakeholder buy in | Key stakeholder support | Stakeholders informed of progress | Review of stakeholder satisfaction | Analysis of stakeholder benefits |
| Quality of project management | Design of project management | Effective team respect timetable | Contract management arrangement | Problem solving arrangement | Post deal evaluation | Effective internal controls |
| Balance of cost, quality and finance | Affordable based on market soundings | Good quality compliant and bankable bids received | Analysis of financing terms for debt & equity | Changes made are value for money | Unitary charge remains affordable | Benchmarking of price and quality |
| Quality of risk management | Analysis of scope for risk transfer | Risk management procedures | Appropriate risk transfer agreed | Management of risk | Risk transfer sticks | Procedures updated |

BUILDING SCHOOLS FOR THE FUTURE (BSF)

showing increase in Senior Debt costs

BSF PFI deals – total interest rates

Percentage



SUBMISSION TO THE ECONOMIC AFFAIRS COMMITTEE OF THE HOUSE OF LORDS ON THE STRENGTHS AND WEAKNESSES OF PPP IN THE UK

October 2009 National Audit Office

Private finance can deliver benefits, but it is not suitable at any price or in every circumstance.

7 Key points follow:

1. Private finance projects normally deliver what is asked of them.
2. Justifications for using private finance are often unclear
3. Institutional incentives encourage the use of private finance
4. Evaluation of the use of private finance is not well developed
5. Good competition is vital to achieve value for money
6. Delivery of real risk transfer depends on a good contract
7. Private finance projects require very careful project management

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