

Criteria for a sustainable development of the toll road concession model in the US

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Jordi Graells
International Toll Roads Manager
Abertis Infraestructuras SA
Barcelona, Spain

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The Scenario

The Message

#1. Feasible Project

#2. Sound Conceptual Framework

#3. Sound Concession Contract

**#4. Selection of a Reliable and Credible
Long Term Private Partner**

#5. Long Term Involvement of State

Final Remarks

- The bulk of the investments needed on the trunk highway network of the country are on existing infrastructure, to offset the insufficient maintenance and capex of the last decades, and to relieve congestion.
- Rehabilitation & reconstruction, capacity and interchange expansion, and ITS plus tolling technology will probably be the main investment items.

- If the private sector must step in to help on these no-greenfield projects, many, or most of the deals will probably be both concessions of existing turnpikes and concessions of currently untolled, to be tolled freeways. Concession frameworks have been in place for more than 40 yrs elsewhere, and have proved to work well.
- This presentation suggests some criteria to States to succeed on this new mission, in the short term and in the long run.

A successful toll road Concession deal in the US will be the result of clear and solid policies set by State:

- #1. Feasible Project**
- #2. Sound conceptual framework**
- #3. Sound Concession Contract**
- #4. Selection of reliable and credible long term private Partner**
- #5. Long term involvement of State on Project**

- Existing traffic must be significant
- Traffic forecasts must be conservative: annual increases $> 5\%$ in first 10 yrs, and annual increases $> 3\%$ afterwards are hardly credible. Should not be credible to financial analysts or bondholders too.
- Initial toll rates must be reasonable (at least 15 cents per mile for cars). Must be increased annually with CPI. More than CPI will quickly prompt rejection by users. Less than CPI will question feasibility.

- O&M expenditures must be coherent with traffic levels and with the quality of service the facility must provide to users at any time, or State will have a problem.
- Therefore, EBITDA/Revenue ratios $> 75\%$ are hardly credible either, at any time.
- The benefits of ETC or open road tolling are essentially to accommodate more traffic in the same toll plaza with better service, not to reduce costs dramatically.

- Initial Concession period should be no more than 35-40 years. Beyond that, no cash flow is worth a penny today.
- If the period is longer, State is really awarding at least two concessions, one of them for free, and State is losing the opportunity to extend concession in the future, in exchange for more Capex in the region or in exchange for revenue sharing.
- Initial Capex engagements must be well defined along concession period.

abertis #2. Sound conceptual framework (1/3)

- State ought to have a champion manager with clear mandate and an excellent in house (small) team, with clear concepts and ideas and a strong will to succeed. Must be protected from bipartisan politics.
- Champion manager to be in charge of definition of project, deal rules, concession contract and Partner selection, under control and approval of political power.
- External consultants are necessary, but will not work efficiently without champion

abertis #2. Sound conceptual framework (2/3)

- Framework to be drawn by benchmarking in depth the real reference success stories: 30+ yr old European concession companies
- State ought to be cautious in falling for a quick buck today, or it may risk buying a severe future problem (with bondholders and thus with constituency).
- State ought to focus on getting steady flow of revenues (money or capex) instead.

abertis #2. Sound conceptual framework (3/3)

- If Concession award is based on a lump sum price, State must consider that a ratio Enterprise Value/Ebitda > 18 (around) is probably neither credible nor sustainable.
- Partner must submit a credible baseline financial statement forecast, with linear asset depreciation (IAS), without equity loss, with positive net profit reached before year 10 and maintained beyond.

- Ought to be comprehensive but simple, setting clear rules and concepts and assigning clear and realistic risks and responsibilities to each party.
- Benchmarked with European concession regulations & contracts
- Risks to be taken by Concession Company: construction cost, traffic (except because of government actions), financial cost, O&M cost, direct taxation, changes in general legislation and regulations.

- Risks to be taken by State: right of way availability, changes of indirect taxation, force majeure consequences, traffic consequences of government actions, consequences of changes in the specific regulations applicable to Concession.
- Renegotiation and compensation mechanisms ought to be built in and rely upon baseline financial statement forecasts submitted with the bid. Final reference parameter must be either free flows IRR or free flows NPV.

#4. Selection of reliable and credible long term private Partner (1/3)

- State ought to select Partner like in a marriage; a shared long term vision, trust, loyalty, diligence and a common ground.
- State ought to select Partner with an integrated, long term vision of its role and a clear commitment to manage full lifecycle facility management (design+build+finance+operate+maintain)

#4. Selection of reliable and credible long term private Partner (2/3)

- State ought to examine management record of Partner carefully for credibility and reliability assessment.
- Partner ought to prove commitment to bring (and maintain) a substantial amount of equity and an efficient and sustainable financial structure.
- Partner ought to have substantial capacity to raise money for project with its own guarantee, without recourse to project.

#4. Selection of reliable and credible long term private Partner (3/3)

- Partner committed to employ all talented people and to use all know-how existing in facility running Authority.
- Partner committed to develop intense interaction with local and business communities in region.
- Partner with a solid record of good working relationships with Government.
- Partner with proven corporate responsibility and environmental record.

- **Two partners, not one: along concession, State has substantial responsibilities and roles with project and with Concession Co.**
- **State to set up control team in charge of responsibilities and roles.**
- **State control team to identify unforeseen capex needs and to renegotiate them with Concession Co.**
- **State to maintain a permanent dialog and collaboration with Concession Co.**

- **Define a feasible project.**
- **Choose the right partner.**
- **Define common sense rules, benchmark on the real toll concession success stories.**
- **Write a contract that can work for 35-40 years. Read contracts in Europe.**
- **Focus on the stream of revenues, not on the quick easy buck.**
- **In short, build a sustainable success story.**