

Public-private partnership: lessons from the COVID 19 pandemic

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Crises have always been treated with investments in life support infrastructure, making it possible to significantly reduce unemployment, strengthen the domestic market, and create attractive conditions for business development. The current crisis is not an exception. Modernization of infrastructure has become one of the priority tasks for almost all countries in the world, and especially for the developing economies. At the same time, the possibilities of the latter to finance infrastructure projects at the expense of public budgets have narrowed (tax revenues have decreased, the costs of supporting the population and business have significantly increased because of COVID 19). As a result, attracting private investment has become an urgent issue.

But is it realistic to initiate PPP projects during a pandemic?

Will private business be ready to get involved in their implementation, and if so, on what terms?

These and other issues are actively discussed in the world today, exposing the current and potential problems of attracting private business for the implementation of long-term large-scale projects, highlighting the pros and cons of this mechanism.

Among the obvious disadvantages of PPP, which arose during the crisis for the projects under implementation, are the violation of the work schedules envisaged by contracts, the decrease in solvent demand for services provided under PPP, or its absence at all (for example, it has happened in the case of airport projects), the narrowing of public budgets capacity to provide timely availability payments. Of course, all these circumstances have seriously complicated the implementation of PPP contracts for private business. At the same time, business that was not involved in PPP projects faced similar problems during the pandemic.

Among the advantages of PPP are the relationships between business and public authorities in force majeure conditions that have been fixed by contracts. Well-prepared contracts clearly define how the obligations of the parties are adjusted if something goes wrong. Accordingly, in general, projects implemented on the basis of PPP turned out to be much more resistant to the crisis than commercial ones, and the reaction of the parties of PPP contracts to the pandemic was quicker. In contrast to purely commercial projects, in PPP the obligations of the parties are fixed on a long-term basis and even in a crisis do not change in essence, but are only slightly amended in accordance with the new circumstances. At the same time, in well-prepared PPP contracts, the obligations of partners are specified on the principles they understand. In this case, business does not need to appeal to the state with request of assistance and patiently wait for at least some kind of reaction to such request. It just has to follow the contract.

In addition, for PPP contracts lasting more than a dozen years, although the suspension of the fulfillment of certain obligations of the parties for six months or a year is critical, it will most likely save the project from collapse. And business opportunities to "hedge" in the case of PPP are much higher than when being in "free float". Any lender would prefer to finance a project with

an understandable long-term perspective, rather than assist a business in a difficult situation, the profitability of which is complicated to assess even in the short term. As a result, the business operating under the PPP conditions is much more protected during the crisis.

It should be noted that for the state as well, the relations with business in the framework of PPP turned out to be not too problematic. Payments by a public partner to compensate for losses of a private partner provided for in PPP contracts are usually not urgent. And the potential for their restructuring in the case of long-term projects is high. At the same time, if the PPP contract provides for the construction of a new asset used on a free basis, budget payments to reimburse the private partner's investments should be made after the asset is put into operation. By this time, the asset created under the PPP will be able to provide additional revenues to the budget, which will mitigate the fiscal risks of the state. For example, a road built in the framework of PPP will cause the development of a new business and increase the income of the existing business in nearby settlements, reducing its logistics costs. As a result, additional sources of income will appear for both the state and local budgets.

The above is mainly related to the existing PPP contracts.

And what about the prospects for PPP development during and after the COVID-19 pandemic?

Will the public authorities become more interested in using this mechanism?

Will private business retain interest in PPPs?

How will the situation develop in this area?

There is no single answer to these questions. It all depends on what conclusions the public authorities will draw from the current situation.

In our opinion, the main conclusion of the pandemic for the state should be that infrastructure projects to implementation of which the private business is invited should be prioritized based on an assessment of their social and economic effect and impact on the quality of life of people. In the conditions of the narrowing of the public budgets potential and the growth of infrastructure needs, it is critically important to select projects that should be implemented in the first place, by including them to state (municipal) infrastructure programs (the so-called "pipeline of projects"). The need for such an approach to the selection of projects is important not only because of the limited resources of public budgets. It is equally important to have the technical ability to implement them, as well as ensure the effective use of time of qualified civil servants who are able to prepare, evaluate and monitor the implementation of PPP projects. This is especially important for the developing economies, whose institutional capacity on PPP issues is usually low.

It should be noted that the formation of pipeline of projects in a crisis conditions with a focus solely on the commercial attractiveness of infrastructure projects does not meet the public interest. Such criteria for assessing the priority of projects are natural for private business, but they are not suitable for public authorities. The state should take care of the common wealth and the development of the territory. Accordingly, in the first place it should be planned to implement the projects that will ensure the creation of the infrastructure most demanded by the population,

eliminate the existing problems and contribute to the sustainable development of the country / settlement.

COVID-19 has demonstrated that preparedness of countries / cities for emergencies, both arising from pandemics and those of a man-made nature, should be included to such priorities. There are many cases in the world for studying the problems that may arise in connection with their occurrence. Although such situations do not arise often, their analysis shows that the costs of eliminating their negative impact on people and territories is much higher than the costs to create a resilient infrastructure that could significantly mitigate or completely avoid severe consequences of emergency situations. And here we are talking not only about reducing losses, but also about preserving people's lives and health.

In this context we observe a positive trend in changing of the public authorities` attitude to the development of medical infrastructure. Recently, there has been a worldwide commercialization of medical services. Not only the profitability, but also the effectiveness of their provision was mainly assessed by the demand for such services by patients. As a result of this approach, the attention to infectious medical institutions has decreased. After all, linking the funding to the number of patients does not work here. The pandemic has demonstrated that modern infectious disease clinics, laboratories and general infectious disease specialists should exist in any state, regardless of the current epidemiological situation. And for this financial resources shall be provided.

Such "reserve" resilient infrastructure assets should be state-owned. But they could be built and maintained by a private business on a PPP basis, receiving a payment from the state (local) budget for this. Moreover, as the current pandemic is likely to last a long time and COVID-19, alas, is not the last pandemic that we will have to face, such an infrastructure must be created quickly. Today, when the resources of public budgets are limited, it is very problematic to create such an infrastructure without involving private business.

Private business has the necessary financial resources and competencies to implement PPP projects. In theory, it is interested in partnership with the state (local government bodies) in the implementation of long-term investment projects, including socially important ones. But the realities are such that business will be ready to invest only in those PPP projects that are commercially attractive and with acceptable risks.

Therefore, an important condition for understanding the future for PPP in a particular country is the willingness of public authorities to ensure acceptable risks for business when implementing infrastructure projects on PPP conditions. And this is possible in the case of an adequate distribution of risks between partners, the existence of mechanisms to guarantee risks arising from the fault of the state partner, as well as clear regulation in the contract of the rules for clarifying the rights and obligations of the parties in the event of force majeure circumstances. When structuring a project as a PPP, it is necessary to assess the most "incredible risks" that may arise in the process of its implementation, as well as to foresee and reflect in the PPP contract the rules for resolving by its parties of any non-standard situations arising during the contact term. To do this, a PPP contract must determine the logic of building relationships between the parties in cases where the occurrence of circumstances that could not be foreseen results in the

impossibility of any party to the contract to fulfill its obligations either in general or for some indefinite period of time.

Equally important is the availability of an understandable and logical system of state support for PPP implementation. Only in this case it could be expected that in the conditions of the crisis, socially important projects will be attractive for private investment. It is not worth hoping that the creation (modernization) of life support infrastructure will pay off solely by consumer payments for services provided in the framework of such projects. This is especially true for the developing economies, for which attracting investment in life support infrastructure is critical in terms of public interest.

A serious obstacle to business participation in long-term investment projects is also the high transaction costs that it incurs in the process of preparing (in the case of unsolicited proposals) and considering proposals for the implementation of PPP projects. The unwillingness of public authorities to understand the new innovative approaches used in PPP, their habit of doing everything "the old fashioned way", as well as the lack of preparation for an equal dialogue with business, either lead to excessive unrealistic expectations when structuring infrastructure projects as PPPs (when such projects are structured by public authorities), or to excessive delays in the process of considering business initiatives (in the case of unsolicited proposals). It must be remembered that for a business, "time wasted" is "lost money." High transaction costs when launching PPP projects "kill" business interest in long-term cooperation with public authorities in the field of infrastructure modernization, even in the case of excellent legislation.

Based on the above, the public authorities should be aware that in conditions of competition for a long-term financial resource, the countries that fail to reduce business transaction costs when preparing and considering PPP projects will be left without private investment in the life support infrastructure, and thereby prolong the crisis for many years... The recipe for overcoming this problem is known - increasing the requirements for the qualifications of the public sector in the field of infrastructure development, in particular on the basis of PPPs, and strengthening control over the performance of civil servants responsible for this area. The task is not easy, but realistic.

In this context, in particular, it is important to ensure prompt and objective consideration of PPP proposals initiated by business (so-called "unsolicited proposals"), if they meet the strategic priorities of the country. Until now, the attitude to such proposals in the world has been restrained. It was believed that business, initiating PPP projects, first of all thinks about its own interests. And therefore, it is better to focus on projects prepared by public authorities, which "think about the people". This, by the way, is not always confirmed in practice.

Today, when it became clear that it would be extremely difficult to get out of the crisis without the participation of private business, and in some countries it would be impossible to prepare PPP project proposals by public authorities that have neither the competencies in this field, nor financial resources to attract consultants who could assist them, the interest of private business to initiate PPP projects should be supported and even stimulated. After all, it is impossible to bridge the investment gap relying only on projects prepared by public authorities in the countries with low institutional capacity of civil servants.

The main thing that needs to be paid attention to in terms of consideration of unsolicited proposals is that the infrastructure planned to be created (subject to modernization) should be in demand by the society and meet the development priorities of the country / territory. In order for unsolicited proposals to meet this requirement, it would be perfect for the state (local government) to familiarize business with its priorities. In simple words, they need to prepare and publish a PPP program, specifying which of the projects included in it could be structured by the state (local government), and for the preparation of which it would be desirable to invite private business. If unsolicited proposals are in line with government priorities, they must be dealt with due care and promptly.

Taking into account the above the following *conclusions regarding the "post-pandemic" future of PPP for the developing economies could be made.*

Life has demonstrated the effectiveness and relevance of the PPP mechanism, especially in crisis situations. Correctly structured long-term PPP projects are able to "smooth out" the "peaks" caused by crises, ensuring the stability and continuity of the implementation of the state (regional) development programs.

In crisis conditions, the demand in life support infrastructure is increasing, the ability of public authorities to provide financing for infrastructure projects is narrowing, and the caution of private business when making investment decisions is growing. All this results in increased competition among countries in attracting infrastructure investors to PPP projects.

Only a country that demonstrates to private business both the interest to cooperate with it in infrastructure modernization and its ability to ensure attractive conditions of partnership will be able to win competition in this market. It should be explained to business:

- what are the state (regional) priorities for the medium and long term perspective;
- proposals on the implementation of which PPP projects it would be interested to receive from private business;
- on what principles and with the use of what mechanisms it is planned to ensure the payback of PPP projects, especially social ones, for private business;
- how the government plans to "ensure" private business implementing PPP projects in the event of materialization of risks that business is not able to influence.

And finally, it is necessary to prove not in words, but in practice that a public authority:

- perceives business as a partner, respects its competencies and values its time;
- is able to speak the same language as a private business;
- resolves all issues in the process of initiating and launching PPP projects quickly, efficiently and in accordance with the procedures prescribed by law.

The latter is extremely important. This is due to the fact that private business, of course, studies the demands of countries in infrastructure, reads laws, listens to promises from the authorities and politicians, BUT makes decisions on starting projects based on the analysis of PPP projects already launched and implemented in the country (city).