Ministry of Finance
Department of Economic Affairs
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Public Private Partnership Appraisal Committee (PPPAC)
21st Meeting on January 7, 2009

Record Note of Discussion

The 21st meeting of the Public Private Partnership Appraisal Committee, chaired by Secretary, Economic Affairs was held on January 7, 2009. The list of participants is annexed.

2. The Chairman welcomed the participants and invited Director (Infrastructure) to present the agenda. Director (Infrastructure) stated that the meeting was in pursuance of the directions of the Committee of Secretaries (CoS) in its meeting held on January 02, 2009, wherein PPPAC had been directed to examine the suggestions made by Department of Road Transport and Highways (DoRTH) for enhancing the viability of the national highways' projects which have either not fared well in the recent bidding exercise or were under bidding process, and submit recommendations in this regard to the CoS.

3. The representative of DEA informed that the Department had undertaken an analysis of the projects which had achieved success in the bidding process (15) as against those, which had not elicited a response (19). An indicator to estimate the intrinsic value of a project had been constructed in terms of the Total Project Cost (TPC) per kilometre per PCU on COD date. The value of this indicator for each of the projects had been examined. The projects where the value of the indicator was less were expected to be more successful on being bid out than those where this value was high. While examining this parameter, it was kept in mind that the projects are not of similar nature, *viz.*, the scope of work varies from four laning to six laning; some projects are already being tolled; while the conditions of other stretches require extensive reconstruction. After examination of the projects and on the basis of the earlier appraisals by PPPAC, the following inferences had been drawn by DEA:

i. There is no direct relationship between Project Cost, PCUs and the success/ failure of the projects.
ii. Overall PCU figures need to be treated with circumspection - section wise analysis was vital. Many sections of the roads did not justify the widening/strengthening proposed for the complete project stretch.
iii. A longer concession period need not lead to a better bid response.

iv. Clear regional bias is discernible - projects in Western and Northern region have generally performed better, while projects in Kerala , Bihar, UP have not received a response.

v. Projects, which are *ab initio* unviable, are taken up on BoT (Toll) on account of Cabinet decisions on the matter which mandate that all projects may be first tested for BOT (Toll) before being undertaken in the annuity or EPC mode. The intrinsically unviable projects have an in-built bias towards failure.

4. A tentative assessment of possible bid response to the 25 NHDP projects under the bidding process was also attempted by DEA.

5. After examination of the projects, the Department had recommended the following for enhancing the viability of the projects and for eliciting a better bid response:

i. Use of New Toll Policy would enhance the project viability

ii. The phasing of the VGF between construction and O&M phases could be collapsed for these projects under consideration with the approval of the competent authority. The entire VGF (upto 40% of the project cost) maybe treated as Capital Grant / Equity support for these NHDP projects subject to minimum equity contribution of 18% of TPC[1] by the Concessionaire to avoid crowding out of equity as well as entry of 'non-stake players' and disbursal of the VGF in conjunction with the loan disbursal after the concessionaire has expended the equity.

iii. *Ab initio* commercially unviable projects may require separate handling since bidding the project is not likely to elicit any interest in the market, especially in the current financial scenario. On the other hand, a failed bid casts a shadow of putative failure on the efforts of the Department.

iv. As prescribed in the guidelines for formulation, appraisal and approval of Central sector PPP projects, the RfP should be issued after appraisal of the project structure and PPPAC clearance.

v. Restrictive clause in RfP, which puts a cap on the number of projects which an eligible bidder is allowed to be pre-qualified/selected for could also be a key reason for bidders' withdrawal / lack of response. The clause may be reconsidered/relaxed especially for these NHDP projects which are being bid out in bulk.

6. Advisor to Deputy Chairman, Planning Commission emphasised that during the appraisal of the project, Planning Commission has repeatedly indicated the requirement of rationalising the cost of the projects; re-examining the Manual of

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[1] On the basis of a 70:30 debt:equity ratio.

Standards and Specifications as well the finalising the project structure based on the traffic projections. He drew attention to the Guidelines for capacity of roads in rural areas issued by Indian Road Congress (IRC) and underlined the need to structure the project in accordance with these guidelines. He emphasised that rationalizing the structures on the project highways was necessary, keeping in mind the overall budgetary ceiling as well as adopting a holistic approach towards the capacity of NHAI to undertake high cost project requiring considerable VGF or annuity payouts. With specific reference to the projects under consideration, the following course of action was recommended:

i. In respect of NHDP Phase-V, which is the flagship programme of the Government, the projects may be restructured so that the estimated VGF requirement for the projects is within 5 to 10 percent of the TPC. Limiting the VGF in this manner would be in line with the approval accorded by CCEA to the programme in its meeting held on October 05, 2006. The phasing of the construction of service lanes and restricting extensive provisioning of underpasses could substantially reduce the costs of the projects. The projects may be bid out after their restructuring for a better bid response.

ii. NHDP Phase-III projects should be structured in accordance with the IRC specifications.

iii. The provision of the VGF as capital grant would contravene the provisions of the MCA. An alternate could be to leave the provision as such (viz. 20 percent of TPC as equity support, and remaining as O&M support) with the NHAI Board examining departures from this on a case to case basis with adequate safeguards (such as bank guarantees) to ensure that projects are not abandoned after disbursal of the VGF/equity support.

7. Member (Finance), NHAI emphasised that every project undertaken by the Organisation was in accordance with specific Government directions. It was a conscious decision of the Government to undertake the establishment of the Golden Quadrilateral (GQ), and its subsequent six laning, even though the traffic did not immediately warrant it, in pursuance of the objective of generating an economic synergy across the country. It is envisaged that a road network of international standards thus established would also result in an 'S-curve' effect, leading to higher traffic and economic impetus. It was emphasised that the specifications observed by NHAI for the projects were in conformity with the specifications prescribed by DoRTH with the approval of the competent authority. The specifications had been finalised to ensure safety on the highways and keeping in mind the requirement of urban/ rural settlements through which the highways traverse.

8. The representative of NHAI informed that the organisation had also undertaken an independent analysis of the performance of the projects recently bid out and reached the following conclusions:

i. For any road project, traffic is generally the only variable, with the location, standards and specifications, financing methodology and regulatory/legal regime being specified upfront. NHAI had estimated that the projects with an average annual daily traffic (AADT) of 10,000 PCUs and more had received a better bid response.

ii. A regional bias was clearly discernible; developers were hesitant to venture into projects in Kerala and Bihar. This was on account of two reasons; first, these were difficult regions in the context of construction difficulties as well as inadequate traffic; and, secondly, the restrictions imposed in the bidding process, earlier at RfQ stage and recently on RfP stage had encouraged 'cherry picking' of more viable projects in economically sound states of Maharashtra, Gujarat, etc.

iii. Out of 35 projects bid out, 16 projects had elicited a response, indicating a success rate of 46%. The response is on account of two positive developments; first, increase in the total project cost of the projects (by 10% and 20% for projects prepared in 2006 and 2007 respectively); and, secondly, improvement in the financial and liquidity conditions which had resulted in reduced interest rates.

9. The representative of NHAI informed that on examination of the issues, the organisation had proposed provision of VGF as capital grant, with disbursal linked to milestones and loan disbursement. The enhancement of concession period was expected to provide greater comfort to the lenders and hence a better bid response. He urged that the proposal for enhancement of the total project costs by 30 percent for projects where DPRs had been prepared in 2006 may be considered favourably to align the project cost with its estimated value, after taking into account the financing costs and interest during construction required for the project till the COD. It was further informed that NHAI was examining the 19 projects which had not received any bid response and would consider their restructuring for enhancing their viability. It was informed that DoRTH had diluted the clause 2.1.18 of the RfP for the projects where the bidding process had not been successful and that NHAI would support relaxation of the clause for the other highway projects.

10. Joint Secretary, Expenditure stated that as suggested by the PPPAC in its 19th meeting, DoE had examined the proposal for enhancement of the TPC of the projects where the DPRs had been prepared in 2006 and 2007. Ideally, the Department would have preferred to undertake a case-by-case analysis of the projects before recommending the proposal. However, due to the urgency of the proposal, the generic issues were examined and the proposal recommended for favourable consideration to the PPPAC and CoS. However, the Department did not support further enhancement of the TPC of the projects prepared in 2006, by 30%, as proposed by DoRTH, without a detailed analysis of individual projects. The matter had been independently examined by the banks, who have noted that there are wide variations in the requirements of increase in the TPC. This also strengthens the need to undertake a project specific assessment before further enhancing their TPC. The Department was supportive of the provision of VGF grant during the construction phase subject to adequate safeguards and the competitive bidding process being followed.

11. Representative of Department of Legal Affairs noted that the Department had not received any specific proposal from the DoRTH. The Department would examine the legal aspect of the policy, formulated subsequent to decision on the matter.

12. The Chairman summarised the deliberations as under:

i. There was broad support to the proposal from DoRTH for disbursal of VGF during the construction stage, linked to equity and loan disbursals. The view of DEA was that the VGF could be provided as equity support, subject to a minimum equity being expended upfront by the concessionaire and the disbursal of VGF being *pari passu* with the disbursal of loan. Planning Commission's view also did not rule out provision of VGF during construction stage with adequate safeguards. However, this change may be specific to the projects under present consideration without entailing an amendment to the Model Concession Agreement.

ii. The proposal for extension of concession period or enhancing TPC may be considered after examination of the requirement of individual projects and not as a generic measure.

iii. Planning Commission has recommended restructuring of the projects for better alignment of the project costs and the expected revenue streams.

iv. DEA had suggested a broad prescription for enhancing the viability of the projects through use of New Toll Policy, reviewing the applicability of the Clause 2.1.18 of RfPs and bidding projects which were identified to be more structurally and commercially robust for an early harvest of successful projects.

v. DoRTH may adopt a more phased approach while bidding out projects.

It was decided to commend the above recommendations and deliberations for consideration by the CoS.

(Action: DEA)

13. The meeting ended with a vote of thanks to the chair.

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List of Participants

I. Department of Economic Affairs

i. Shri Ashok Chawla, Secretary (Economic Affairs) (In Chair)
ii. Shri Govind Mohan, Director
iii. Ms. Aparna Bhatia, Joint Director
iv. Ms. Prathibha A, Deputy Director

II. Department of Expenditure

v. Ms. Rita Menon, Special Secretary
vi. Ms. Meena Aggarwal, Joint Secretary

III. Planning Commission

vii. Shri Gajendra Haldea, Adviser to Dy. Chairman
viii. Shri Ravi Mittal, Adviser
ix. Shri S.P. Chouhan, Director

IV. Ministry of Law

x. Ms. Poonam Suri, Legal Counsel

V. Department of Road Transport & Highways

xi. Shri Brahm Dutt, Secretary
xii. Shri P.K. Tripathy, Joint Secretary
xiii. Shri Nirmal Jit Singh, Additional DG

VI. National Highways Authority of India

xiv. Dr. A. Didar Singh, Member (Finance)
xv. Shri S.K. Puri, Member(Technical)
xvi. Shri M.P. Sharma, CGM
xvii. Shri G. Suresh, GM