PPP: Cue Norway

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Norway has finally joined the ranks of Nordic PPP practitioners in earnest with a three-deal pilot PPP programme. The three pilot projects are all in the road sector and will involve the upgrade of the Klett to Bardshaug (in Sor-Trondelag county) and Lyngdal to Flekkefjord (in Vest-Agder county) sections of the E39 motorway and the Grimstad to Kristiansand (in Aust-Agder county) section of the E18 motorway.

The deals have been some time coming ? the Norwegian parliament included the plans in the 1998 budget ? but the preferred bidder for the first deal has now been announced and funding should be closed by the end of this month. Ernst and Young advised the Norwegian government on the programme. And while the regions' earlier proponents of PPP may now have cooled somewhat on the concept, industry experts are hoping that Norway's three-deal package may spur renewed enthusiasm for PPP across the region.

In developing its PPP model, Norway has placed significant importance on achieving the cost-effective implementation of its political goals for road usage: ?Good accessibility with a high level of traffic safety for a road network with the objective to unite the country without causing unnecessary damage to the environment.?

The first deal will involve the Klett to Bardshaug section of the E39 to the west of the country. The NK1.5 billion (Eu210 million) project has been awarded to the Orkdalsleden consortium, which is made up of Skanska BOT and Laing Investments as contractors with around NK1.3 billion project debt arranged by LB Kiel and Nordea. Three other bidding consortia included Bouygues of France, Hochtief of Germany and Sweden's NCC respectively. Parties understood to have shown interest on the debt side include Depfa Bank and Sumitomo. The Orkdalsleden consortium will design and build a new road from Oysand to Thamshamn.

Dr Ansgar Benidek, director and head of infrastructure finance at LB Kiel in Germany, describes the financing as a back-to-back structure with a construction period of around three years. ?The original discussions did consider both loan and bond options but the potential for early repayment by Vegvesen (or Vegdirektoratet ? Norway's public roads administration) meant that a bond issue was not the best way to go.?

The loan itself is in three tranches and runs for 1.5 years less than the 25-year operational concession awarded by Vegvesen. The three-bank underwriting group for the syndication is in place, with Svenska Handelsbanken having joined the two arrangers for a 25% slot. LB Kiel is underwriting 50% of the loan and Nordea the balance. Benidek describes the pricing as ?aggressive? at 100bp over Libor during the construction phase and a 15bp step-down to 85 bp over Libor post-construction.

?The major risk in a project like this is construction and the important issue here was the willingness of the construction companies to absorb risk,? says Benidek. ?Contractors within Norway are generally happy to take such risk.? Construction of the roadway will be undertaken by Skanska subsidiary Selmer Skanska and it is understood that on completion the Norwegian government will reimburse roughly one third of the upfront construction costs as a subsidy.

The project itself involves a 27km section of new build on a twisting section of coast road which is notorious within the country for its low quality and high accident rate. It has short curves, low visibility and few options for overtaking. The scheme also involves the construction of 10km of tunnels. It is the state of roads such as this one that explains Norway's decision to site all three of its pilot PPP schemes in the same sector. ?PPP projects are now being considered in other sectors such as prisons and schools, but when the scheme was introduced the roads sector was more relevant for the politicians, as it was the sector in which there was the greatest need,? explains Kersti Billehaug, manager of the PPP programme at Vegvesen.

The Ministry of Transport and Communications originally put forward two projects in its National Transport Plan but this was subsequently increased to the current three deals. Billehaug explains that having three projects in the same sector provides a useful learning curve. ?The three projects are in different parts of the country,? she explains. ?It is important to take them in stages as these are very large deals for the Norwegian market and could not be financed at the same time.? The Klett to Bardshaug E39 deals is the first to be done as it was the most advanced in terms of planning.

Any country adopting PPP technology will clearly look to some extent at the UK as a blueprint, but Vegvesen also had other examples of PPP schemes closer to home to draw from. The pioneer for motorway projects in the region is the Helsinki to Lahti scheme in Finland. This 69km road project involved the construction of 88 new bridges and was completed 11.5 months ahead of schedule in 1999. The project was undertaken by the Tieyhtio Nelostie Oy consortium of which Skanska BOT and Laing Investments were members. The FMK 290 million project debt was arranged by Sampo Bank and Nordic Investment Bank. ?The Lahti project was a practical example of PPP being implemented in the Nordic region,? notes Gunnar Westerlund at Helsinki-based law firm Roschier Holmberg. ?But the success of the scheme raised the expectation that there would be a lot of follow-up projects which there haven't been. The Norwegian approach seems more sensible. By putting three road projects into one package they have created a systematic approach [to PPP],? he says.

Vegvesen versus Lahti structure

The Vegvesen road projects are, however, fundamentally different from the Lahti scheme. The former had a shadow toll structure whereas the E39 scheme involves real tolls ? a feature that many industry observers considered highly unlikely in Norway. But the Norwegian schemes will involve a unitary payment from the state on an annual basis ? effectively removing any real traffic or tolling risk from the projects. The real tolls are collected by a not-for-profit government entity ? E39 Oysand ? Thamshamn A/S ? and are used as a base for the annual unitary payments. ?Our scheme will differ from other models as the payment mechanism is far more predictable,? explains Billehaug at Vegvesen.

The unitary payment is split into availability and performance based payments and has been designed to maintain the same standards on the privately financed highways as those on the state system. ?We want to make sure that standards are the same as those on the state-owned highway ? the government does not want to cede control over the highway network,? says Billehaug. Norway has strict maintenance procedures ? such as snow clearance within two hours. The payment structure also involves bonus payouts for improvements in safety. E39 Oysand ? Thamshamn A/S has entered into a separate agreement with Vegvesen to regulate how toll funding will be used to partly finance road development.

The most important task for Vegvesen was not to take elements from other PPP structures but to craft something that is uniquely Norwegian. This they seem to have achieved. ?The PPP process is more focused and streamlined than that in the UK,? notes Benidek at LB Kiel. But he adds that the process was helped by the fact that Norwegian law is well suited to the concept. Billehaug at Vegvesen explains that some adjustment to the interpretation of tax and VAT rules was needed but that these were minor. ?The most difficult part of the whole process was bringing people who have experience from different kinds of deals to the new model,? she explains. This involved taking experience from the UK model and those with experience of more traditional Norwegian deals and changing their thinking to encompass the new payment scheme. ?We had to get everyone together and create something new and Norwegian and not English,? she says.

?The Norwegians have a very strong preference that PPP should be adapted for Norway,? agrees Westerlund at Roschier Holmberg. ?They are trying to create a local approach and have made a strong effort to reduce the size of the documentation,? he says. There seems to be a real sense of frustration in Finland that the success of Lahti has yet to be built on and it will be interesting to see whether Norway's more structured approach delivers efficiency gains sufficient to trigger adoption of PPP in other sectors.

The first major railroad PPP scheme in Scandinavia was Sweden's Arlandabanen project which closed in 1995. This BOT scheme was used to construct a high-speed airport link in Stockholm ? the contractor was NCC. A similar airport link deal is now under consideration in Helsinki. ?Everyone [in the Nordic region] is aware that this [PPP] can be done and can be done efficiently,? notes Westerlund. ?It is no longer necessary to show that it can be done ? this has already been proven.?

Rival to UK PPP volume?

But adoption of PPP on the scale that has been seen in the UK is still questionable in the region, given the relative conservatism of Nordic governments in the financing of social welfare schemes. For this reason, any further near-term projects are likely to be rooted in the road and rail sectors. The Norwegian pilot schemes are therefore being looked to as a potential boost for the PPP concept across the region.

?Vegvesen have a very good understanding of the PPP process and support within Norway for PPP is good,? comments Benidek at LB Kiel. ?This will hopefully foster PPP across Scandinavia,? he says. But while support for the concept of PPP is growing, each country seems determined to adopt its own model and the degree to which any genuine private sector risk is considered is still a long way from PPP models in use elsewhere in Europe.

In Denmark, while PPP has been keenly debated, the major infrastructure projects undertaken so far ? such as the Great Belt Crossing and the Oresund Crossing to Sweden ? have been publicly funded or carried the full guarantee of the Danish state. In Sweden, despite the landmark Arlandabanen deal, PPP has become a politically contentious issue and no mention of it was made in the Swedish Infrastructure Bill published in October 2001. Indeed, government funding has been designated for several large rail and road projects such as the Malmo City Tunnel and the Uppsala motorway project (a proposed PPP road project).

The Orkdalsleden consortium prequalified for the E39 deal early in 2002 and best and final offers were submitted in December. But the two further pilot road projects have yet to reach the pre-qualification stage. While Skanska BOT and Laing Investments are clearly in a very strong position with their experience on the Lahti project and this concession, it remains to be seen whether the Norwegian government will want to stick with this consortium for the other deals or diversify its project sponsors.

Initial submissions for the second project ? the second stretch of the E39 to be upgraded between Lyngdal and Flekkefjord ? were made on January 15 and attracted five bidding groups. These are the Laing and Skanska BOT team; NCC, Bilfinger Berger, and Egis; Veidekke; Strabag, AF Gruppen and Bouygues, AS Anlegg and AS Vegproduksjon ? the state-owned road maintenance agency. Debt arrangers have yet to be named but there are strong indications that LB Kiel and Nordea may arrange the debt portion for the second deal. The second E39 deal is expected to be roughly the same size as the first but the third pilot road project ? the E18 deal ? will be far larger. The E39 Lyngdal to Flekkefjord project will involve 17.5km of new road, 7.5km of tunnels and several new bridges including a bridge over the Fedafjord, Birkeland Bridge and Refsti Bridge.