Queensland Motorways

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The Global Projects Center (GPC) is an interdisciplinary research center at Stanford University that seeks to facilitate understanding of the financing, developing and governance of strategic infrastructure assets. We conduct research on infrastructure **finance**, **development**, and **investment**.
Background on Concession Financing of Brownfield Assets
Concession Financing – U.S. Example

Chicago Skyway
- 2004: RFQ
- 10x respondents
- 5x selected to compete
- 99 year concession to collect tolls
- Fixed tolling schedule

What is the value of the Chicago Skyway?

Complete Responses
- Abertis Infrastructure: $505mm
- Vinci: ~$700mm
- Cintra/Macquarie: $1.83bn
Hurdles for Concession Financing

Chicago Skyway Ex-Post Re-valuation

Figure 3

Chicago Skyway Transaction
Projected Increased Revenues (Net Present Value)
Revenues Available to repay Franchise Fee of $1.80 Billion

<table>
<thead>
<tr>
<th>Annual Traffic Growth</th>
<th>With 2% Floor</th>
<th>With 3% CPI</th>
<th>With 4% GDP</th>
<th>With 5.5% GDP</th>
<th>With 7% GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>No Growth</td>
<td>$1.47</td>
<td>$1.92</td>
<td>$2.60</td>
<td>$4.48</td>
<td>$8.62</td>
</tr>
<tr>
<td>Historic Growth (3.78%)</td>
<td>$8.37</td>
<td>$13.08</td>
<td>$21.59</td>
<td>$49.89</td>
<td>$124.72</td>
</tr>
<tr>
<td>Moderate Growth (2%)</td>
<td>$3.48</td>
<td>$4.93</td>
<td>$7.36</td>
<td>$14.85</td>
<td>$33.26</td>
</tr>
<tr>
<td>Aggressive Growth (5%)</td>
<td>$16.63</td>
<td>$27.85</td>
<td>$48.90</td>
<td>$121.97</td>
<td>$322.38</td>
</tr>
</tbody>
</table>

$322bn lost Gross Revenue!

Source: Enright, The Chicago Skyway Sale: An Analytical Review

- Cost of Equity (Corporate Profit v. Public Funding)
  - Includes Risk

- Ex-post project re-valuation
  - Does not include Risk
The Costs and Benefits of Concession Financing

Drivers of Value Creation in Concession Financing

- Risk Transfer
- Governance Change
  - Long Term Management
  - Stranded Assets
  - Opportunity for Innovation / Practice Changes

Impediments to Concession Financing

- Valuation
- Transaction Costs – an impediment to competition
- Value Capture
  - Corporate Profit v. Public Funding
Queensland Motorway Transaction
Queensland Motorway Transaction

State Financial Situation

- Deteriorating Balance Sheet post-GFC
- Ratings Downgrade
- Unfunded Pension Liability

2009 Proposal to Sell Concession

- Proceeds for Pension Liability Payment
- Significant Public Response
- Question of Correct Valuation

Concession Proposal Public Responses

It is possible that the private sector could attempt to extract excess returns for taking on the ownership or management of public assets. This would be an income transfer from taxpayers to the private sector equity holders and therefore not in the general interests of taxpayers.

<table>
<thead>
<tr>
<th>Table 1. NPV calculations</th>
</tr>
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<tbody>
<tr>
<td>Revenue growth (real)</td>
</tr>
<tr>
<td>------------------------</td>
</tr>
<tr>
<td>Baseline</td>
</tr>
<tr>
<td>Low revenue growth (2.5%)</td>
</tr>
<tr>
<td>High revenue growth (5%)</td>
</tr>
<tr>
<td>High discount (5%)</td>
</tr>
<tr>
<td>Low discount (2%)</td>
</tr>
<tr>
<td>Short period (n=30)</td>
</tr>
<tr>
<td>Long period (n=50)</td>
</tr>
</tbody>
</table>

Source: Guest, RACQ
QML Transfer to State Defined-Benefit Pension

2010: Queensland government begins negotiations for in-kind contribution of QML to defined-benefit pension

Queensland Investment Corporation (QIC): government-owned corporation that manages defined-benefit pension
- Independent board of directors
- Infrastructure allocation includes direct investment team – staff with capability to assess and manage investments

**Transfer Process**
- Arms-length negotiation
- Valuations commissioned by government and QIC independently
- Additional 3rd party valuation commissioned by pension board to verify negotiated valuation
- Transfer completed in May 2011 with $3.088bn valuation, 40 year concession
QML Operations Post-Transfer

Four Year Operating Changes

- Senior Management Changes – incentives tied to performance
- New tolling technologies installed
- Maintenance Management Plan developed
- Financial reporting systems overhauled
- Acquisitions: CLEM7 Tunnel, Legacy Way, Go Between Bridge

Timeline: Acquisition of Legacy Way and Go Between Bridge from Brisbane City

1. Timeline
   - Initial Approach to BCC by QIC regarding their toll road assets, September 2012
   - Commercial agreement reached 15 July 2013 ("Memorandum of Understanding")
   - Contract close 12 September 2013
   - GBD financial close 24 December 2013
   - LW financial close expected June 2015

2. Process
   - Due Diligence
     - QML/QIC performed technical due diligence on
       - Traffic
       - Cost base and capital expenditure
       - Toll structuring
   - Collaboration and negotiation
     - Structure of transaction required collaboration regarding business plan, assumptions and optimizing structure
     - Range of consideration structure developed by QIC to achieve BCC and QIC objectives
     - Agreed financial model between parties
     - Negotiation of term sheet including commercial items and risks allocation
   - Commercial documentation finalized
     - Agreed term sheets translated into critical transaction documents
       - Framework and transaction deed
       - Concession deeds
   - Operating forecasts and commercial term sheet negotiated and agreed
   - Long form legal agreement drafted
   - Conditions Precedents satisfied
QML 2016 Sale by QIC

- Portfolio balancing problem as QML valuation increased
  - System size and revenue increased
  - EBITDA Margins increased 8%
- QIC decision to divest to rebalance portfolio
  - Winning Tender: $7.4bn (Transurban, AusSuper, ADIA)

QML Value Realization 2011-2016

- Capital Invested: $3,088
- Additional equity for acquisitions: $488
- Total capital invested by DB Fund: $3,576
- Cash distributions: $388
- 2014 monetization EV: $7,057
- Less: CLEM7 debt: ($270)
- Total capital returned to DB Fund: $7,375
- Value realized: $3,798
Key Takeaways and Requirements

Requirements

• Government capability to manage concession infrastructure procurement – Value for Money
• Independent Pension Decision Making (Arm’s Length Transaction)
  • Governance: Independent Board, Fiduciary Responsibility
  • Capability: Internal or Sourced capability to assess and manage investment
• Complete Process Transparency

Value Drivers

• Governance Transition
  • Tied to pension capability / incentives to manage effectively
• Public Value Capture: Overcoming valuation difficulty in infrastructure market
Questions?

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