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PPP Case Study: Long-Term Concession for Bourgas And Varna Airports, Bulgaria

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The Challenge and the Opportunity





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The Project Structure

Project Development and Implementation Support

- Stage 1: Pre-feasibility, legal due diligence and options assessment
- Stage 2: Framework Preparation; Transaction Structuring
- Stage 3: Transaction Implementation
- Stage 4: Contract Negotiation and Financial Closure

Commitment to Capacity Development and Awareness:

- Extensive engagement, formal training, awareness and media education

Resource Commitment:

- From USAID: resident + short-term technical advisors, local professional team + small procurements
- From MoT: Concessions Department and key personnel throughout MoT + + cost sharing of key procurements + Int'l legal advisors procurement and direct transaction costs



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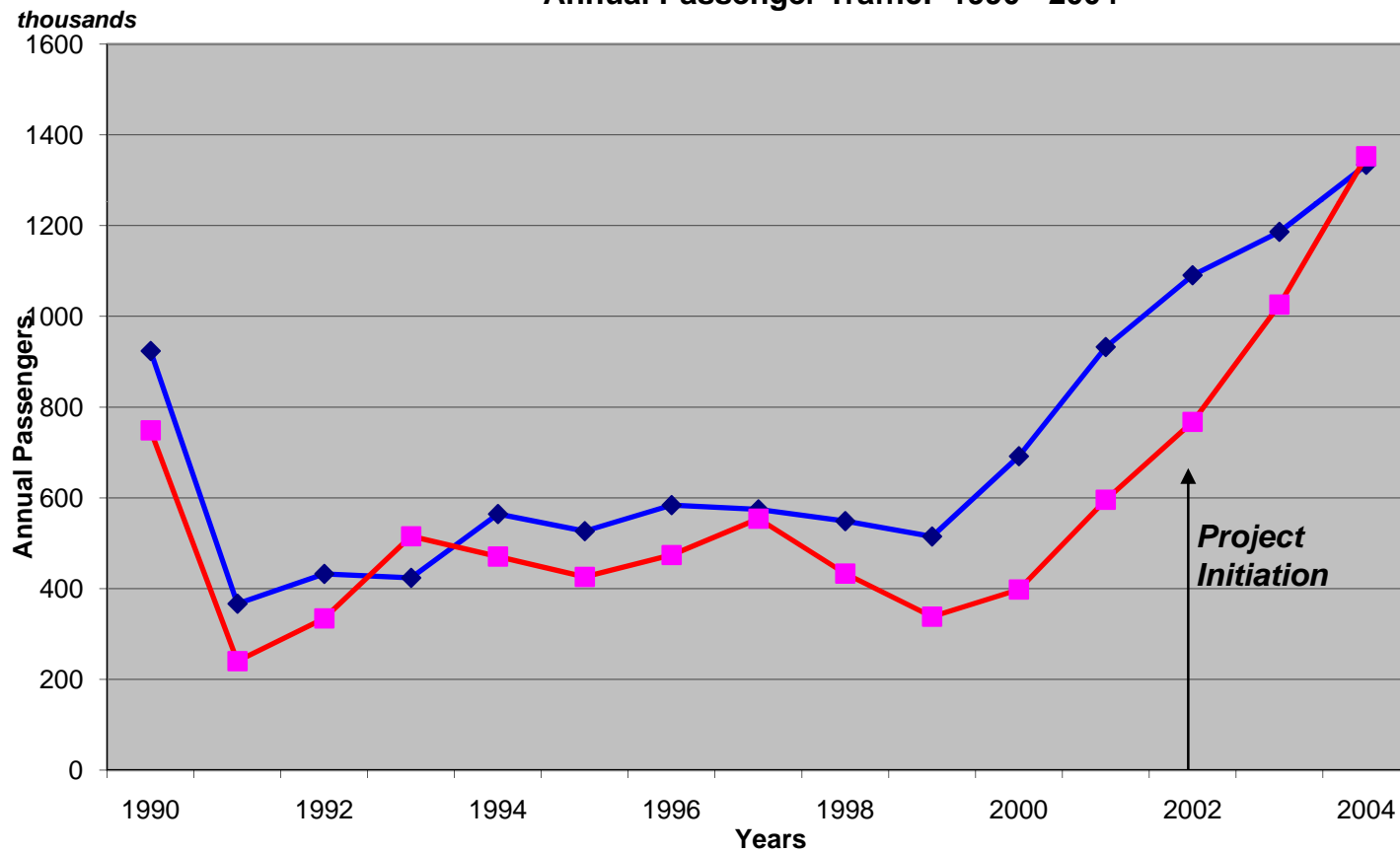
Stage I: Preliminary Due Diligence

- Legal Due Diligence:
 - Immediate problem with Civil Aviation Act
- Environmental and Social Due Diligence
- Technical and Financial Due Diligence:
 - Developed traffic forecasts and capital expenditure plan for 10-years
 - Financial modeling, including operating and financing costs
 - Issue: To bundle the airports
- Way Forward:
 - Prepare amendments to Civil Aviation Act
 - Design concession in line with Law on Concessions
 - Prepare concession analyses and transaction documentation



Bourgas and Varna Airports

Annual Passenger Traffic: 1990 - 2004





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Illustration of Capacity Constraints





Airport Capacity, Sample at Varna Airport

Observed August 12, 2002	Actual Area (sq. m)	PAX	Actual sq.m/PAX	Lev/Serv E [IATA]		Lev/Serv C [IATA]	
				Target sq.m/PAX	Area Reqd. sq.m	Target sq.m/PAX	Area Reqd. sq.m
Check-In Area	384						
1540-1620		1002	0.38	1.0	1002	1.4	1403
1650-1800		1158	0.33	1.0	1158	1.4	1621
1800-1840		745	0.52	1.0	745	1.4	1043
Baggage Claim Area	250						
1450-1553		826	0.30	1.2	991	1.6	1322
1626-1723		1184	0.21	1.2	1421	1.6	1894
1751-1834		816	0.31	1.2	979	1.6	1306
1900-1939		877	0.29	1.2	1052	1.6	1403
Immigration	400	1184	0.34	0.60	710	1.00	1184
Level C: Good level of service, conditions of stable flow, acceptable delays, good level of comfort							
Level E: Inadequate level of service, condition of unstable flow, unacceptable delays, inadequate level of comfort							
Service below Level E considered as SYSTEM BREAKDOWN							

Based on terminal capacity alone and at current traffic levels, the airports regularly provide no quality of service, classified internationally as SYSTEM BREAKDOWN.



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Economic Impact of Airports:

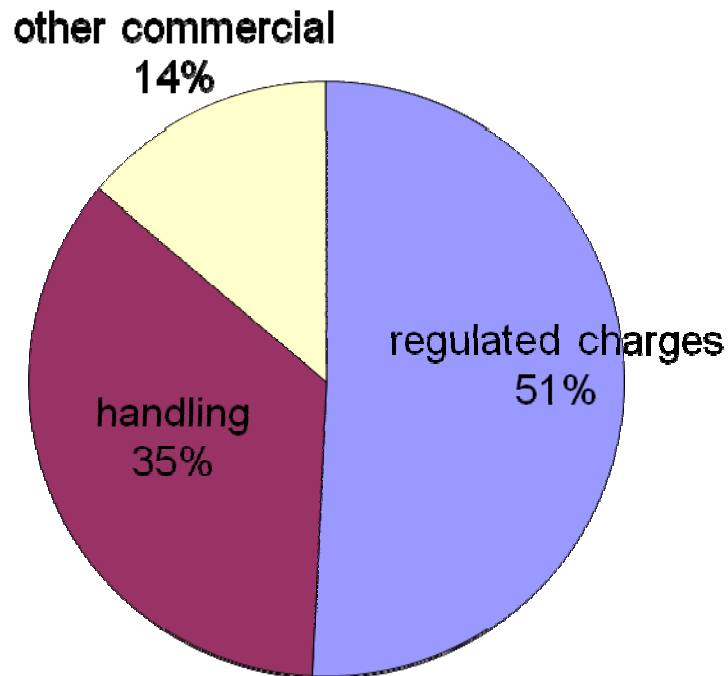
“Studies suggest that failure to increase capacity to meet demand could reduce GDP at regional and national level by 2.5 to 3%”

Source: Airports Council International, The Social and Economic Impact of Airports in Europe, January 2004



Little Commercial Orientation:

Breakdown of Airport Revenues, 2004





Multiplier Effects from an Increase in Passenger Traffic

Example: Dynamic airport management could easily result in an increase in traffic, conservatively estimated at 1% per year additional traffic growth.

1% increase in airport traffic = 10,000 new tourists

7 tourists = 1 job

10,000 tourists = **1,400 jobs in the service industry**

JOBS

1 tourist = €450 spent in BG

10,000 tourists = **€4.5M spent throughout BG**

MONEY

1 tourist = 7 bed-nights

10,000 tourists = **70,000 additional bed-nights**

70,000 beds/200 nights season =
350 beds fully occupied per season

REGIONAL DEVELOPMENT

This is an example of the annual economic benefits that Bulgaria can realize solely from improved airport management and operation.



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Government Objectives for the Airports Project:

- ✓ To facilitate immediate investments in airport infrastructure without State financing or guarantees.
- ✓ To improve the quality of airport services.
- ✓ To promote the development of commercial activities.
- ✓ To ensure efficient, cost-based provision of airport infrastructure and related services.
- ✓ To transfer commercial risks related to airport operation and investment.
- ✓ To maximize overall State budgetary revenues (fees, taxes, etc.), inclusive of capital investment program.



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Airport PPP Options

AIRPORT PSP OPTIONS					
	1	2	3	4	5
OPTIONS	Service Contract	Management Contract	Lease	Concession	Sale
Ownership	Public	Public	Public	Public	Private
Investment	Public	Public	Public	Private	Private
Management	Public	Private	Private	Private	Private
Operation	Public/ Private	Private	Private	Private	Private
Risk	Public	Public/ Private	Public/ Private	Public/ Private	Private
Remuneration	Fee, usually fixed price	Fee, usually performance related	Profits from operations. Lessee pays rent to public sector for use of assets. Can be fixed or revenue/volume linked	Profits from operations. Concessionaire pays fee to public sector for use of assets. Can be fixed or revenue/volume linked	Sales proceeds to Government
Examples	1. Maintenance and operation of several remote and isolated airports in Canada. 2. Aer Rianta's retail contracts in Pakistan, Bahrain, Kuwait, Beijing, Beirut, etc.	1. BAA - Port Louis Int'l Airport, Mauritius. 2. Aéroport de Paris - Marsa Alam Airport, Egypt. 3. ACSA - Pildanesburg Regional Airport, South Africa.	YVRAS Ltd - Fort St-John, Kamloops, Canbrook Regional Airports, Canada.	1. Aeropuertos Argentina 2000 - 33 airports in Argentina. 2. TBI plc - Cochabamba, Santa Cruz and La Paz Int'l Airports in Bolivia.	1. BAA plc (7 airport in the UK) 2. TBI plc - Cardiff, Wales



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Stage II: Legal, Institutional and Transaction Preparation

- Parliament
 - Amendment to CAA passed through entire legal process
- Stakeholder Awareness
 - Ministry and key government personnel
 - Airport management and employees
 - Clients: airlines and tour operators
 - Media
- Transaction Design
 - Knowledge of international experience essential
 - Extensive informal market feedback
 - Getting regulation right



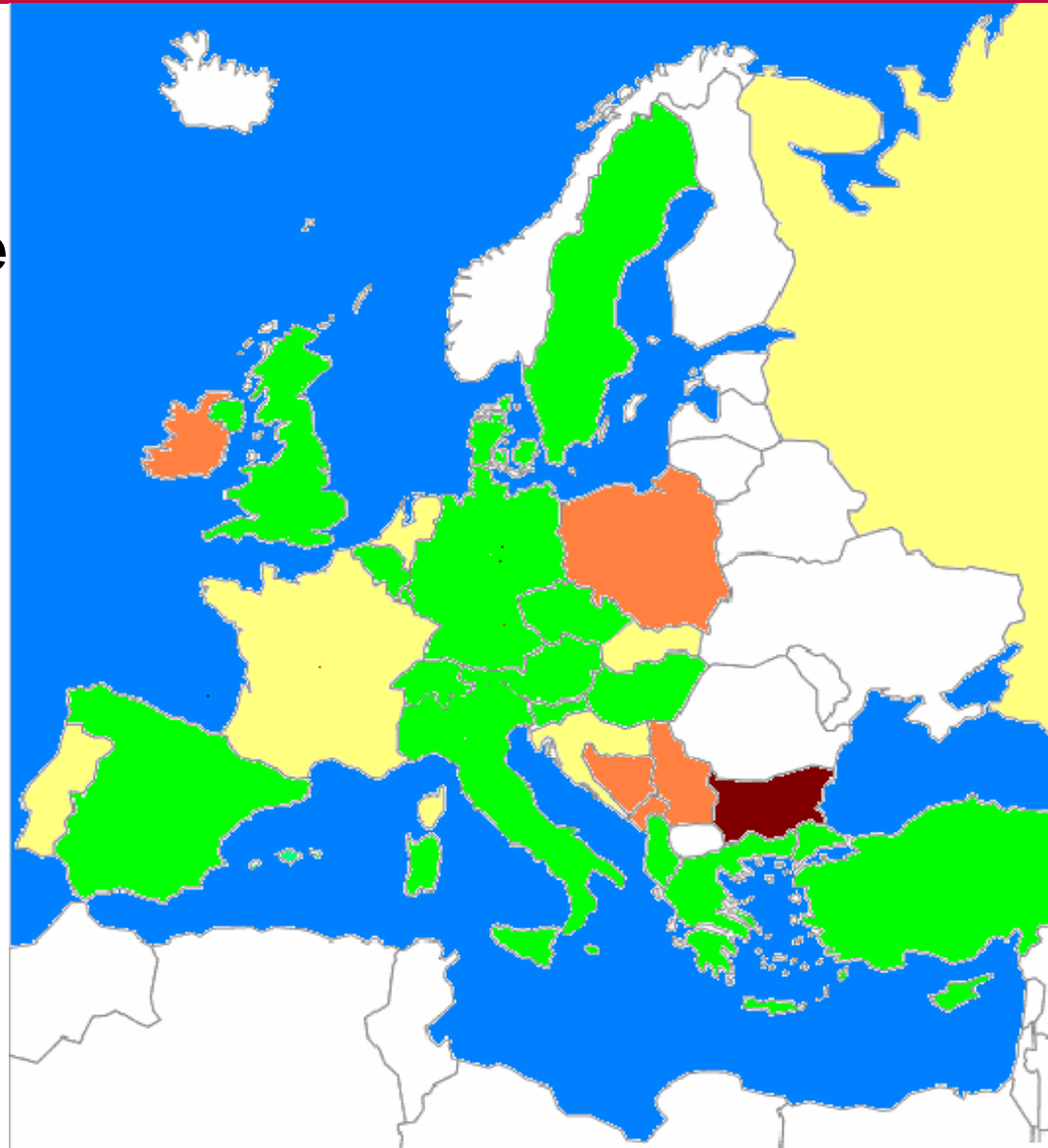
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**Relevant experience:
European experience
was key for Bulgaria**

Key:

- Green:** Significant Airport PPP
- Yellow:** Decision taken
- Orange:** Considering





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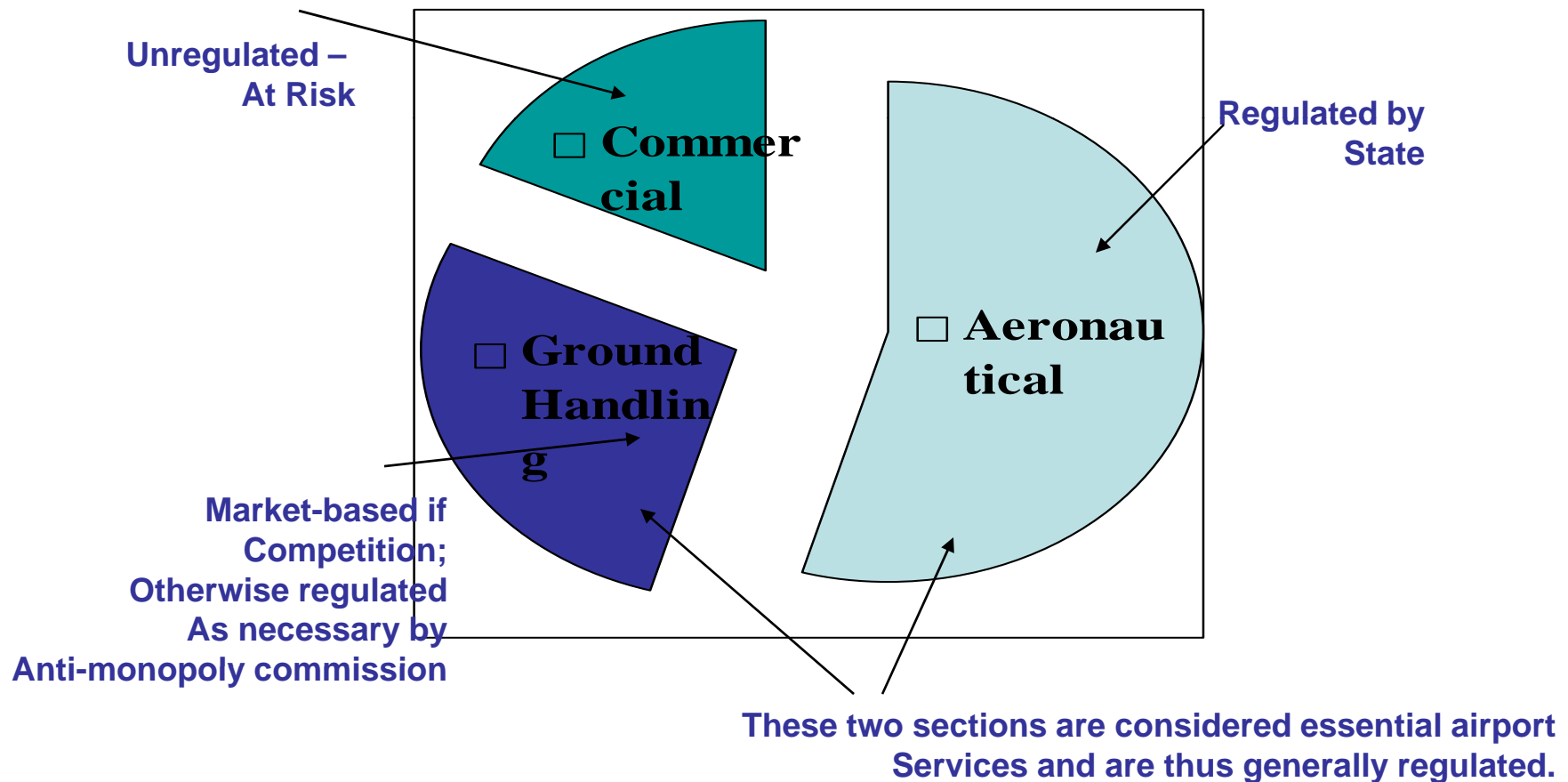


Relevant Transaction Experience

	RECOMMENDED	SELECTED PREVIOUS INTERNATIONAL CONCESSIONS								
	BOURGAS/VARNA BULGARIA	LARNACA CYPRUS	ROME ITALY	ATHENS GREECE	LUTON UK	ISTANBUL TURKEY	MALTA	AUSTRALIA	ASUR MEXICO	LIMA PERU
TENDER STRUCTURE										
capex requirement	service-driven with set minimum	service-driven	service-driven	BOT tender	service-driven	BOT tender	service-driven	service-driven	service-driven	set minimum
capex bid	binding bid with final MP approval	binding bid	none	bid binding EPC	indicative bid subject to MP	EPC bid	none	indicative bid subject to MP	binding bid subject to MP	binding bid
aeronautical opex	at cost with efficiency factor	at risk	at cost	at cost	at cost	at risk	at cost	at cost with efficiency factor	at cost with efficiency factor	at risk
concession fee	bid % gross rev. annual	bid % gross rev. annual	10% gross rev. annual	none n.a.	bid upfront	none n.a.	bid upfront	bid upfront	5% gross rev. annual	bid % gross rev. annual
aeronautical ROI	implicit in bid	implicit in bid	regulator set	implicit in bid	implicit in bid	implicit in bid	regulator set	price cap	price cap	price cap
user fees in bid	Y1-Y5 preset, indicative Y6-Y35	preset	none	indicative bid	indicative bid	preset	none	preset Y1-Y5	preset Y1-Y5	preset
rate making	cost-plus	cost-plus	cost-plus	cost-plus	market	fixed	cost-plus	cost-plus	cost-plus	fixed
period	5-year rolling per masterplan	term	by decree	unregulated	one year	bid	by decree	5-year rolling	5-year rolling	term
CONSORTIUM STRUCTURE										
min. paid-in equity	EUR 20M	set min.	bid	bid	bid	bid	bid	bid	bid	\$40 Million
min. operator share	25%	set min.	none	bid with TSA	none	bid with TSA	bid with TSA	bid with TSA	25% with TSA	15% with TSA
SELECTION METHOD										
technical bid	scored	ranked	none	scored	scored	pass/fail	scored	pass/fail	pass/fail	scored
financial bid	scored	ranked	ranked	scored	ranked	ranked	scored	ranked	ranked	scored
combined	weighted	sequential	n.a.	weighted	weighted	sequential	weighted	sequential	sequential	weighted



Regulatory Approach: Dual Till Principles and Cost-Recovery





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Transaction Structure:

- ✓ Long-term master concession for 35 years, airports bundled together.
- ✓ Development of master plan by Concessionaire for approval by State.
- ✓ Significant near-term investment requirements, specified as key inputs to be delivered by Concessionaire.
- ✓ Ongoing minimum quality of service targets (output-driven)
- ✓ Dual-till regulation, with aeronautical till regulated by the State on a cost-recovery basis, with efficiency factor.
- ✓ Concession fees paid to State on gross revenues (aeronautical and commercial).
- ✓ Core ground handling activities provided by Concessionaire.
- ✓ Airports employees transferred to Concessionaire.



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Stage III: The Transaction

- **Prequalification Process**
 - Arguably, the most important part of the transaction
 - Specific technical requirements: multiple countries, minimum PAX and managed investment, consortium membership
- **Tender Implementation**
 - Extensive due diligence
 - Dialogue process on draft concession agreement
- **Proposal assessment**
 - Clear scoring criteria
 - Recognition of binding and non-binding proposal elements



Market Knowledge

COMPANY	HOME	PASSENGERS			AIRPORTS		RECENT INVESTMENT	DIRECT EMPLOYEES	REVENUES EURO	CREDIT RATING MOODY/(S&P)	OWNERSHIP
		TOTAL	AT LARGEST AIRPORT	AT SECOND AIRPORT	TOTAL	ABROAD					
AENA	ES	154M	35M	23M	47	11	>1MM		>1MM	-	STATE
ADP	FR	71M	48M	23M	20	18	678M		>1MM	(AAA)	STATE
ADR	IT	40M	20M	10M	11	9	>1MM	2,269	456M	/(BBB+)	MACQUARIE/LISTED
AER RIANTA	IRL	52M	15M	15M	6	3	?		420M	/(A)	STATE
ALTERRA	UK	12M	6M	4.5M	6	6	140M		N.A.	-	PRIVATE J.V.
BAA	UK	200M	63M	29M	20	12	>1MM	11,861	>3MM	A3/(A+)	100% LISTED
BIAC	BE	15M	15M	N.A.	1	0	PIER A	763	256M	-	30% BE INVESTORS
CEPA VEOLIA	FR	0	0	0	0	0			100M	Baa1/	100% LISTED
COPENHAGEN	DK	37M	18M	5M	13	12	120M	1,347	290M	/(A)	70% LISTED
FERROVIAL	ES	41M	24M	5M	13	13	325M	28,000	450M	-	100% LISTED
FRAPORT	DE	70M	48M	10M	6	2	>1MM	21,400	2MM	-	70% LISTED
HOCHTIEF	DE	60M	24M	15M	4	2	720M	4,400	1MM	-	100% LISTED
SCHIPHOL	NE	59M	40M	13M	6	2	>1MM	2,231	860M	Aa3/(AA-)	STATE
(AA2000)/SEA	IT	(9M)/25M	(4.5M)/20M	(4M)/5M	(32)/2	(0)/0	(100M)/>1MM		(-11M)/N.A.	-	(PRVT)/LOCAL GOV'T
TBI	UK	16M	6.6M	3.7M	8	5	30M	1,887	265M	-	100% LISTED
UNIQUE	SW	18M	17M	<1M	4	3	300M	1,425	355M	/(BBB)	45% FREE FLOAT
YVRAS	CA	30M	15M	5M	14	9	200M		N.A.	/(AA-)	LOCAL GOV'T/CDC
VIENNA	AU	30M	14M	12M	3	2	>50M?	2,600	320M	-	50% LISTED
VINCI	FR	50M	24M	10M	26	26	120M		500M	Baa1/	100% LISTED
WIGGINS	UK	<1M	<1M	<1M	6	5	15M	200	(27M)	-	100% LISTED



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Tender Documentation

TENDER DOCUMENTS			
Stage	Document	Availability to Public	Purpose
	Announcement letter	Open	Market the impending tender to the industry
1	Terms of Reference and Application <i>including:</i>	Open	Describe tender process and rules applying to interested parties
	Request for Qualifications		
	Indicative Transaction Summary		
	Confidentiality Agreement		
	Letter of Invitation	Directly to admitted applicants	Informs selected bidders on procedures for entering next stage (signing CA, purchasing docs, scheduling site and data room visits)
2	Information Memorandum	Qualified bidders only	Give potential bidders sufficient information to produce binding proposals
	Data Room documentation <i>including:</i>	Qualified bidders only	Give potential bidders sufficient information to produce binding proposals
	Legal Analysis		
	Airport layout and planning docs		
	Detailed historic airport financials		
Asset lists			
	Request for Proposals <i>including:</i>	Qualified bidders only	Provide bidders with required contents of bid, bid submission rules
	Transaction assumptions		Give bidders necessary guidance to produce bid
	Bid Bond draft language		Provide bidders with guidance on posting bid bond
	Financial Pro Forma Templates		Provide uniform means for submission of forecasted financial information
	Technical Pro Forma Template		Provide uniform means for submission planning specifications
	Draft Concession Agreement	Qualified bidders only	Provide opportunity for bidders to give feedback in advance of bid submission



Clear Scoring Criteria

WEIGHTING OF PROPOSAL SECTIONS

Technical Offer		60%		
1. Management Proposal		30%		18.00%
Commercial Plan	25%		4.50%	
Human Resources and Social Plan	25%		4.50%	
Operating and Maintenance Plan	25%		4.50%	
Transition Plan	25%		4.50%	
	100%			
2. Investment Proposal		50%		30.00%
Ability of proposed solutions and phasing to meet capacity needs	70%		21.00%	
Funding Plan (equity and committed debt)	15%		4.50%	
Level of specificity and feasibility of demand and cost assumptions	15%		4.50%	
	100%			
3. Financial Pro Forma Templates		100%	20%	12.00%
Reasonableness and impact of indicative user fees				12.00%
Financial Offer			40%	40.00%
Concession fee percentage		100%		40.00%
		100%	100%	100%
				100% ²²



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Key Bidding Challenge: How to limit the impact of concession fees on user charges?

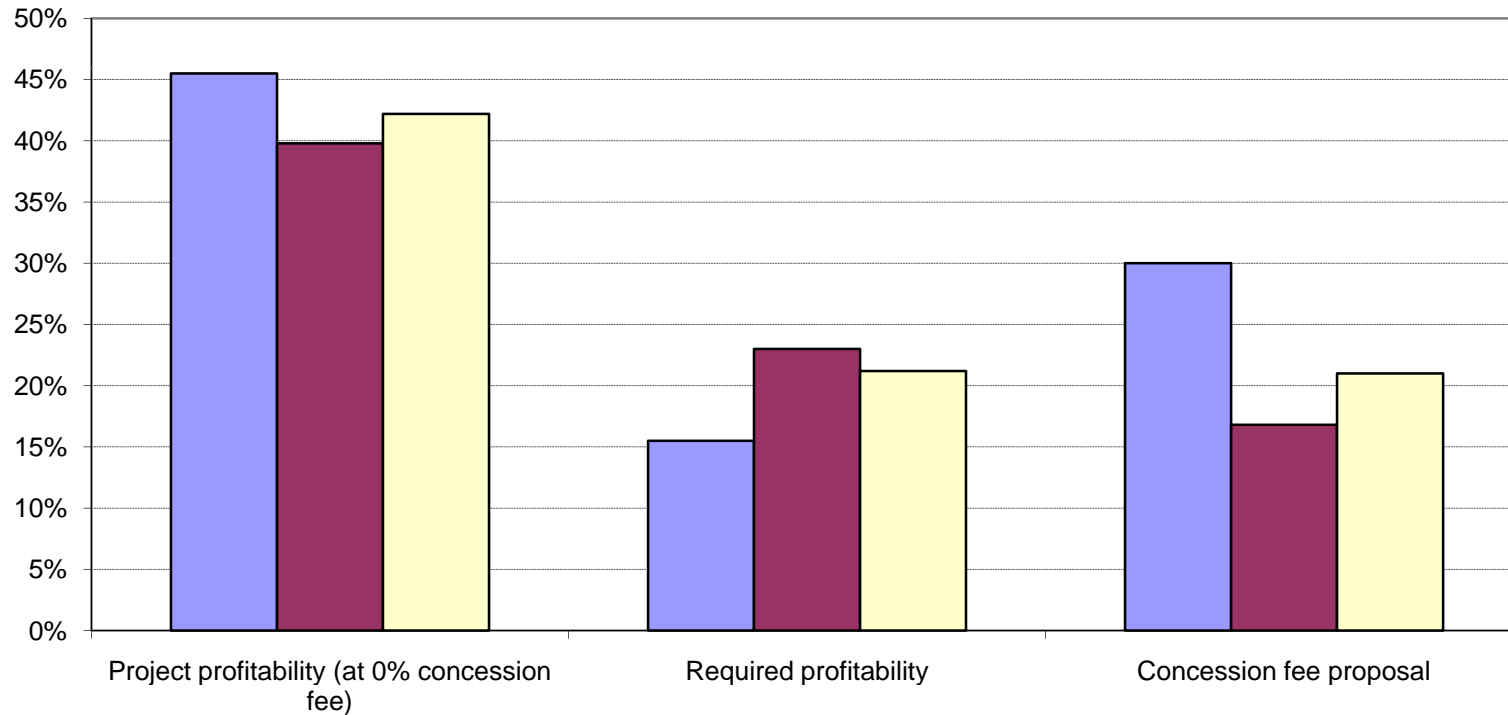
- Concession fees become an operating cost for the airport, reimbursed through rate setting.
- Higher concession fees = higher user charges.
- Desire to 'cap' concession fees, thereby limiting their impact on charges.

The response:

$$\text{Concession Fees (\%)} + \text{Return on Equity (\%)} = \text{Fixed Number (Set by State)}$$



Comparison of Financial Proposals:





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Conclusion: Results and Impact

- Completed Transaction:
 - Fraport-led Consortium took over the airports in 2006 – 60% of Bulgaria’s international air passengers:
 - 19.7% concession fee + 530 million USD capital investment (front-loaded)
 - Commitment to int’l service standards
 - No increase in regulated charges projected
 - Projected near-term doubling of commercial activities at the airport (from less than 15% of gross revenues to nearly 30%)
- Capacity in MoT and experience/exposure throughout Government
- Roll out of more concession transactions:
 - 10 seaport transactions initiated, plus 2 more airport concessions for regional airports
- Follow-on changes to the Concession Law and implementing procedures

1.5 million USAID investment: 1 billion USD transaction



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Critical Success Factors

- ✓ Exceptional prequalification process
- ✓ Selection of appropriate early-stage PPP transaction
- ✓ Focus by Ministry on pilot transaction
- ✓ Senior leadership and staff commitment
- ✓ Commitment to stakeholder awareness efforts
- ✓ Advisory commitment to mentoring and capacity building



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Lessons Learned

- A political commitment and engagement is critical:
 - Political support to enabling environment
 - Management of multiple actors
- Sophisticated understandings of unique PPP issues is required by decision-makers:
 - Step-in rights for lenders
 - Recognition of corporate experience
 - SPVs and consortia behavior
- Post-transaction issues require greater attention:
 - Contract monitoring
 - Regulatory responsibilities



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Thank you