

**WORKSHOP ON PUBLIC PRIVATE
PARTNERSHIPS
FOR OFFICIALS FROM RCCs, METROPOLITAN,
MUNICIPAL AND DISTRICT ASSEMBLIES**

**ASSESSING AND MANAGING RISKS IN PPP
ARRANGEMENTS**

BY

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Introduction

- A key action in a PPP arrangement is the identification and mitigation of risks
- The efficient and effective way of identifying and managing the risks is a way to show whether a project will succeed or not
- International best practices shows that risk identification and mitigation is thus a very important aspect in any PPP arrangement
- The first step toward structuring a PPP is often to put together a comprehensive list of all the risks associated with the project. Such a list is known as a Risk Register.




Definition of Risk

- Risk is defined as the measurable probability that the actual outcome will deviate from the expected or most likely outcome.
- Risk is also defined as the unpredictable variation in the project's value – from the point of view of some or all stakeholders – arising from a given underlying 'risk factor'.




Identifying Risks

- Risks associated with PPPs vary depending on the nature of the project. However certain risks are common to many types of PPP projects.
 - Risks are identified during the feasibility studies carried out as part of the project preparation process
 - The nature of a project determines the type of risk(s) associated with it.
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Categories of Risks

Risk Category	Risk Category	Risk Category	Risk Category	Risk Category
Commercial/Finance	Site	Meeting Standards	Political	Operations and Maintenance
Market Demand or Volume Risk	Site Inaccessibility Risk	Funding Risk	Change in Political Leadership Risk	Operation Cost Risk
Change in Tax Risk	Unavailability of Land Risk	Foreign Exchange Risk	Change in Legal Framework Risk	Maintenance Risk
Financial Risk		Interest Rate Risk	Regulatory Risk	
Sponsor Risk		Insurance Risk	Change in Tax	Force Majeure
Asset Ownership Risk		Environmental Risk		
		Technical Risk		


Risk Allocation and Principles

- Allocation of risk in the context of a PPP means deciding which party to the PPP contract will bear the cost (or reap the benefit) of a change in project outcomes arising from each risk factor.
 - Allocating project risk well is one of the main ways that PPPs can be achieved better value for money.
 - The first is to create incentives for the parties to manage risk well
 - The second is to reduce the overall cost of project risk by “insuring” parties against risks they are happy to bear.
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Risk Allocation and Principles 2

- A central principle of risk allocation is that each risk should be allocated to whoever can manage it best.
 - The risk is allocated to the party best able to **control the likelihood** of the risk occurring
 - The risk is allocated to the party able to **control the impact** of the risk on project outcomes
 - The risk is allocated to the party able to **absorb the risk at lowest cost**
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Response to Risks

- **Risk avoidance** – whereby the source of risk is eliminated or is altogether bypassed by avoiding projects that are exposed to it
 - **Risk prevention** – whereby actors work to reduce the probability of risk or mute its impact
 - **Risk Insurance** – whereby an actor buys an insurance plan – a common form of financial risk transfer
 - **Risk transfer** – whereby actors relocate risks to parties who can best manage them
 - **Risk retention** – whereby risk is retained because risk management costs are greater
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Limitation on Risk Allocation

- Level of detail of risk allocation – Risks are allocated in group but depending on the project type some sub-items can be removed or reallocated.
 - Risks that cannot be transferred – the risk that the government will renege on the contract or expropriate the assets. Private Entities take Insurance at High Cost which in most cases are added to the project cost
 - Extent of risk transfer to private party – equity holders of the private party to the PPP contract – the PPP company/**SPV** – are only exposed up to the value of their equity stake. That is the extent to which risk can be transferred is limited by the level of equity in the project company
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Risk Mitigation Instruments


- These are financial instruments that transfer certain defined risks from project financiers to credit worthy third parties that have a better capacity to accept such risks.
 - The Instruments include;
 - Credit Guarantees
 - Export Credit Guarantees or Insurance
 - Political Risk Guarantees or Insurance
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Risk Allocation Matrix

Risk	Description	Consequences	Mitigation	Allocation
The category and name of the potential risk	How the risk looks like	The potential effect of the risk	How the project plans to deal with the risk if it occurs	The party that can effectively handle the risk



Summary/Conclusion

- Identifying potential risks is a critical aspect of PPP processes
 - The identified potential risks have to be allocated to the party that can best manage it
 - There should be plans to respond to the potential risks identified and this should depend on the existing situation
 - The essence of risk mitigation is to minimise the effect of the risk or eliminate it completely if the risk occurs in the course of implementing the project.
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THANK YOU

