ALTERNATIVE FINANCING AND CONTRACTING MODELS APPLIED BY KENYA RURAL ROADS AUTHORITY

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Presentation Overview

1) Introduction
2) Alternative Financing & Contracting Models
   a) Public Private Partnerships
   b) Low Volume Sealed based Roads 10,000 Programme
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3) Conclusion

1. Introduction

- Development of modern infrastructure is at the core to achievement of:
  a) Sustainable Development Goals (SDGs)
  b) Kenya's Vision 2030
- GoK has prioritized upgrading of 10,000Km of roads critical in supporting the primary growth sectors in the next 5 years.
- Traditional financing and contracting models are unlikely to deliver this target.

Introduction …

- Kenya’s paved road network is only 14,000km after over 50 years.
- **Challenges:**

(i) Budgetary and time constraints. With an average of Kshs 60 - 80M per Km, Kshs 600B - 800B is required in 5years.

(ii) Due to low traffic volumes, many rural roads are unlikely to attract private financing.

Introduction …

- A bulky of the 10,000km is under the jurisdiction of KeRRA
- This has pushed the Authority to explore the following alternative instruments:

(i) Public Private Partnerships (PPP),

(ii) Low Volume Seal Based Roads 10,000 Programme, and

(iii) Performance Based Contracting (PBC).

2 (a) Public Private Partnership (PPP)

- "… a private party (PP) undertakes to perform a public function or provide a service on behalf of the contracting authority" (GoK, 2013).
- In return, the PP benefits either by

(i) way of compensation from a public fund, or

(ii) by charging user fees for service provided, or

(iii) a combination of both.

Public Private Partnership …

- The PP is liable for risks arising from the performance of the function.
- PP required to attain and maintain set service levels thus balancing the public and private interests.
- A single PP is responsible for performing all or a significant number of functions.

Application of PPP by KeRRA

- KeRRA is applying the annuity-based PPP model to implement Ngong – Kiserian – Isinya & Kajiado – Imaroro Roads (91km) – Lot 33 @ Kshs 18.2B

(i) Project Agreement signed in Nov, 2016;

(ii) Financial Close reached in Feb, 2018;

(iii) Independent Engineer is in place;

(iv) Appointed date 21st May 2018

(v) Mobilization currently underway

PPPs – Challenges …

- Lengthy and delicate negotiations over matters not entirely within KeRRA's control.
- Considerable uncertainty in satisfying many contract conditions precedent e.g.
    a) obtaining government approvals,
    b) domiciliation of risks,
    c) sorting out land issues.
- Risk of losing the support of project advisors with fixed price contracts.

PPPs – Challenges

- ❑ Supporting institutional structures not yet robust.
  - PPP Act enacted in 2013 & Regulations released in Oct. 2014
  - Road Annuity Fund Regulations released on April 2015
- ❑ Insufficient competition for PPP tenders
- ❑ Inadequate and attractive local long-term financing (6-10 years)
- ❑ Doubts on sustainability of PPP deals. Guarantees generate significant contingent liabilities

2 (b). Low Volume Seal Based Roads 10,000 Programme

- ❑ Aims at achieving a substantial leap in delivery roads in a cost-effective and timely manner
- ❑ Key characteristics:
  - a) Optimal engineering design;
  - b) Milestone-based contracts;
  - c) A hybrid model - harnesses both public and private capital; and
  - d) Performance Based Routine Maintenance (3years) after DLP

Roads 10,000 Programme - Rationale

a) Kenya has **a large backlog** of roads in need of construction, and maintenance.

b) There is a **huge funding gap** to address the backlog.

c) **Overdesign** of roads with low traffic loading 250,000 to 1M CESA.

d) **No pavement structures** for traffic loading below 250,000 CESA **except improvement to gravel standards**.

e) **Unsustainability** of (re)gravelling of roads

Roads 10,000 Programme - Progress

- Publication of Pavement Design Guidelines for LVSR
- Relaxation of Geometric Design Standards leading to significant reduction in costs
- Currently, the Authority has:
  a) 122 ongoing contracts covering 5,159Kms at a cost of **Kshs 233B**
  b) 137 projects of 4,167Kms worth **Kshs 168B** under procurement.
  c) Physical progress achieved is **1,100km**.

Availability Requirements for R10,000 Programme

IPC No.	Milestone (% of Project Length)	Valuation	Recovery of Advance Payment
1	Advance payment guarantee	10% of Contract Sum	
2	10%	Full value of Works as measured	
3	20%	”	Start recovery as Per Contract
4	30%	”	
5	40%	”	
6	50%	”	
7	80%	”	End recovery as per Contract
8	100%	”	

Benefits of Blended Finance Mechanism

- Ensures a win – win situation.
  a) Incentive for a contractor to perform since significant amount of money is at stake all the time.
  b) Ensures lower private financing component thus:
  - ✓ shields the contractor from excessive "financial exposure"
  - ✓ reduces contractor's premium for such risk hence low prices

Roads 10,000 Programme - Challenges

- A large-scale programme being implemented within very short time frame,
- low contracting capacity,
- inadequate financing, and
- narrow design traffic bands increase probability of under-design
- Axle over loading

R10,000 Programme - Recommendations

- Need for more research on alternative road construction materials.
- Enhancing capacity of axle load monitoring units.
- Strengthening project supervision teams. Even seasoned contractors have not fully understood the LVS approach.

2 (c). Performance Based Contracting - PBC

- Based on fixed lump-sum prices per Km per month for bringing a road to required service levels and sustaining the same.
- Traditional method is **unit rate based and is** a **one-off work package**.
- PBC applies the principle of “paying for services rather than inputs”.
- Monthly lump-sum remuneration covers maintenance services provided, except for unforeseen emergency works.

PBC …

- Contractor bears significantly more risks.
- Optimal transfer of risk and responsibility
- Ultimate goal is to obtain value for money.

- Failure to meet the set minimum performance standards will result in:
  - (i) accumulation of non-compliance points
  - (ii) deduction of monthly payment

PBC …

- KeRRA commenced PBC in 2010
- Over 1,200km of roads are now under PBC
- The network is set to increase drastically on completion of projects under R10,000 Programme.

PBC …

Challenge:

- ❑ Identification, quantification and pricing of risks is based on probabilities.

Way Forward:

- ❑ Enhance capacity building initiatives to all relevant stakeholders.
- ❑ Strengthening Axle Load Monitoring Units is key to success PBC.

3. Conclusion

- ❑No default best financing and contracting option.
- ❑Choice depends on government’s objective given a set of constraints presented by each option.
- ❑ If the objective is fast delivery, choice would weigh heavily on public funds.
- ❑Where there is budgetary constraint, private financing would be the best option.

END

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