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Assessing Commercial Viability

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Once a project is established as viable, the next step is to determine whether it would be attractive to the market if structured as a PPP. Generally speaking, private parties will find a project commercially attractive if it offers good financial returns and requires the private party to bear reasonable levels of risk.

Assessing returns typically involves **financial analysis**—that is, building a project financial model and checking project cash flows, returns, and financial robustness. The **ADB's PPP Handbook** (ADB 2008, 17–18) gives a brief overview of typical financial analysis of a PPP. **Yescombe's chapter on financial structuring** (Yescombe 2007) provides a more comprehensive description.

Where revenue from user charges exceeds costs and yield sufficient returns to remunerate capital, the project will generally be commercially attractive provided risks are reasonable. Where user charges are not at this level, government can use the financial model to assess what government contributions will be needed. Such contributions need to be integrated in financial analysis to assess what government contributions that will be needed—which in turn needs to be assessed as part of the fiscal analysis discussed in Assessing Fiscal Implications of a PPP Project.

Governments often assess the **appetite of potential partners** for a proposed PPP before taking it to market. This can be determined by investigating whether similar projects have previously been implemented with private partners, in the country or the region. It can also include testing market interest through **market sounding**—that is, presenting the main parameters of the project to selected potential investors for questions and comments—typically the project concept and initial structure developed during the structuring phase described in Structuring PPP Projects. The following resources provide more guidance on market sounding:

- **Farquharson et al's chapter on managing the interface with the private sector** (Farquharson et al. 2011, Chapter 8), which includes top 10 tips for a successful market-sounding exercise
- **4ps paper on soft market testing** (4ps 2007), which includes tips, practical guidance, and a case study of a market sounding exercise for a PPP in the United Kingdom
- **Grimsey and Lewis' chapter on procurements options analysis** (Grimsey and Lewis 2009, 409–411), which describes a market sounding exercise for a hypothetical hospital PPP project
- **Singapore's PPP Handbook** (SG 2012, 56–57), which requires implementing agencies to conduct market sounding before pre-qualification, and describes the type of information that should be shared at this stage
- The **Caribbean PPP Toolkit** (Caribbean 2017, Module 5, Section 5), which offers guidance on marketing PPP projects

Market sounding may be done by government agencies directly or may be delegated to transaction advisors. Experienced transaction advisors tend to know the most likely bidders for many kinds of PPP projects—using them to assess market interest allows government to take advantage of these relationships. Market feedback can be more honest and specific when the consultation is conducted by transaction advisors. A government agency may not have the same industry expertise nor the same capacity to engage in a candid dialogue with market participants.

Where local experienced transaction advisors are not available, governments may hire international advisors that have a track record of closing transactions in the specific sector, or perhaps multilateral financial organizations, such as **IFC PPP advisory services.** Transaction costs may be financed by the various

preparation facilities, such as the **Multilateral Investment Fund** PPP advisory facility of the Inter-American Development Bank (MIF) or the **Global Infrastructure Facility** (GIF 2017). These facilities offer advisory services in preparing and structuring PPPs to both attract private sector investment in emerging markets and uphold government project objectives.

Related Content

- **INTRODUCTION**
- **PPP BASICS: WHAT AND WHY**
- **ESTABLISHING THE PPP FRAMEWORK**
- **PPP CYCLE**
- **Identifying PPP Projects**
- **Appraising Potential PPP Projects**
- **Structuring PPP Projects**
- **Designing PPP Contracts**
- **Managing PPP Transactions**
- **Managing PPP Contracts**
- **Dealing with Unsolicited Proposals**
- **Key References - PPP Cycle**

Additional Resources

- Intercreditor Arrangements
- Financial Intermediaries

Find in pdf at PPP Reference Guide - PPP Cycle or visit the PPP Online Reference Guide section to find out more.

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