Ontario – an unholy trinity…

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When it comes to approval ratings for PPP programmes, few markets hold a candle to Ontario. It is revered for being the one to do it right from the get-go, creating a clock-work procurement model and true partnerships with the private sector to deliver public infrastructure – even if it stole the idea from Partnerships BC.

Praises have been sung to the province ever since Infrastructure Ontario was created a little more than a decade ago by private sector specialists who designed a procurement process whereby everyone got a good deal and projects were delivered to a strict timescale.

Perish the thought that the key driver was that these same people were incentivised by bonuses to stick to schedules in a wonderfully metronomic system.

They even closed a deal the day after Lehman Brothers' collapse which confirms the robust nature of the procurement system… and that folk will do pretty much anything to nail down a bonus.

It was this approach by IO – applying private sector principles to the public sector, in addition to hiring in a bunch of bankers and financial advisers – that made Ontario the poster child of the international PPP community.

But is that all about to change?

Ontario now finds itself at a fork in the road, taking it perilously close – were it to take a step in the wrong direction – to "doing a UK"… something that no infrastructure market wants.

In truth, perhaps it's more of a parallel with the Dutch market where all the low hanging fruit has been harvested – pretty much all the vanilla PPPs procured. Now, if the programme is to continue, Ontario must turn to more challenging transactions that are less suited to the cookie-cutter approach that can be applied to schools and hospitals.

So – what now, Ontario?

Anurag Gupta – currently global lead for power at KPMG in London, but previously senior manager at Infrastructure Ontario during its ramp-up years – puts it nicely when he says: "IO finds itself at a point of time where it has built up this incredible expertise of delivery and standardised documentation. But its template product is probably nearing an end. There are only so many hospitals and courthouses you can re-build."

So now IO is faced with the issue of how to develop the more – shall we say – exotic projects. This includes the likes of:

- water and wastewater
- energy from waste
- greening of the energy production space
- relief airport for Toronto Pearson International
- motorway culverts and small bridges

- infra requirements for First Nation communities
- distributed generation and storage in remote communities
- smart infra (electric vehicle charging points)

Ach, the list is long and on the horizon there is a heap of civil / transit DBFM work. This year has already seen Ontario reach financial close on the King's Highway 427 Extension PPP and there is a swathe of light rail projects working their way through the system:

- Hurontario LRT – latest story
- Finch West LRT – latest story
- Hamilton LRT – latest story
- Trillium LRT – latest story
- Confederation Line – latest story

There is also an expectation in the next couple of years that electrification of the commuter rail system around the city of Toronto will progress, not to mention a bunch of rail and railway station upgrade projects.

As to water and wastewater projects, these will be procured at municipal level and their size makes it difficult for them to progress as DBFMs. Efforts by IO to bundle these small and diverse deals has been challenging. However, PPP Canada will be bolstering them with grants of up to 25% to guide them down the PPP route.

But the bottom line has to be that the cookie-cutter PPP model will struggle to work on such a diverse range of projects.

From the mistakes of others…

It's at times like these – a tipping point in a PPP market – that it pays to take a time-out and make sure that your next move is the right one.

Ontario would do well to learn from the UK experience where a world-leading model was leveraged to great effect… right up to the point where it fell from favour – with so much still to achieve.

Ontario remains (for now) determined to continue along the PPP path and drive investment into national infrastructure.

Ryan Greer, director of transport and infrastructure policy at The Canadian Chamber of Commerce, says: "The federal government has put aside a lot of money for the provinces over next decade to tap into water/wastewater and there are going to be a lot of projects in that space."

As Greer points out, big transit projects will continue apace and soon (from November) such transactions will bask in additional support from the C$35 billion Canada Infrastructure Bank… not that there is lack of lending capacity on the ground.

Greer adds: "There is going to be a little more variety and uncertainty as not only does this new institution establish itself, but the province works out what the give-and-take is going to be with the feds on the new federal funding that they are setting up."

Transit projects are receiving greatest focus from a federal level with the government recognising the need to invest in this space to allow manufacturers to move their products around.

"Canada can look substantially different a decade from now when you consider all the money that is going to flow," says Greer.

However, it's not going to be as easy as it was and it looks like IO executives will to work a lot harder to secure their bonuses!

Martin Lavoie at Desjardins says: "The flow has been a little less predictable than in the past and there are now more challenging deals on the horizon. The big, federal projects are a long time in the making and they are few and far between."

Lavoie adds: "The pipeline has been shifting for the last two-to-three years towards civil and there is still a huge pipeline in Ontario – mostly DB and DBF projects. The province has been careful with its budgeting and they are trying to limit use of the DBFM model to where it really matters."

At least there's a sure-thing lender…

The question that has caused more grey hairs and frustration around the global market is lending capacity. To date – even through the worst of the GFC years – Canadian projects sailed through to financial close, enjoying a market that was not as badly savaged as may others (possibly because it hadn't been doing quite so many stupid things prior to the crash).

In this brave new world, sources of lending always have to be investigated, but lo… another one breasts the horizon… and this one's awash with federal cash for Canadian projects.

The impending Canada Infrastructure Bank joins the likes of the UK's Green Investment Bank – now flogged to Macquarie, a decision that will haunt us all one day – and HM Treasury's UK Guarantees which sits within the Infrastructure & Projects Authority (under Steve Lomas and Matthew Vickerstaff respectively), units with bloated staff and keen as mustard to crowd out commercial lenders… if only there were some projects.

As to the Canadian infra bank, it has been taking a leaf out of Australia Infrastructure Bank's book and – together – they may have something to teach US president Donald Trump who is mulling the creation his own infra bank to help his infra plan off the drawing board.

As an aside, the US infra bank is an excellent idea and will help knit together [forgive the cliché] the 50 different markets that make up the US, which – if supported by a broadening of the application of TIFIA loans – could get this frustrating market moving.

And the US definitely needs a nudge in the right direction with Global Infrastructure Hub revealing this week that the US is likely to invest $8.5 trillion in infrastructure from 2016 to 2040, but that its actual needs are 45% higher at $12.4 trillion.

But in Canada's case, the argument for such a bank is less compelling and has resulted in a host of questions at federal level.

Word on the ground is broadly in support of the creation of Canada Infrastructure Bank and, as one source points out, Infrastructure Canada lacks policy / analytical capacity.

"Infrastructure Canada does not have a lot of horsepower," says the source. "It is more focused on administering agreements with other levels of government. For a country like Canada, while we have very strong systems of public infrastructure, we don't spend a lot of time thinking what our greatest needs are, what our priorities are, what some of the supply chain implications are – heading out east, west, or down south toward the US."

He adds: "I am most interested in the analytical horsepower that a bank like this can bring. It may take a few years for it to find its pace, but greatest value would be achieved by bringing people into government with a level of expertise on the deal side that right now – frankly – the feds don't have.

"On the deal side, we are just going to have to see what incremental activity happens as a result of the bank being created and we can judge it afterwards. But I'm hopeful that it can bring intellectual capital to the federal government that it currently does not have."

As with the creation of all such institutions, the first question that leaps to one's lips has to be – is that going to crowd out commercial lenders?

Another source close to the Canadian government says: "I don't think so. I think the government is taking its time over this – and it has already spent a lot of time with the financial community – which is very much Bill Morneau's background.

"He has been doing his due diligence and was down in Australia a few weeks ago to assess what worked with its infrastructure bank, and what did not work. But until it is up and operational, we won't know. They are putting themselves through the paces to ensure it is not something the market doesn't need or crowds out the banks."

One source on the ground reckons that the creation of the infra bank will make it possible for the huge Canadian pension funds to get involved, hopefully bringing to market projects of sufficient scale to attract the big-ticket players.

"The federal government believes that the infra bank will give the pension funds a tool that will help to look at some of these mega projects of which – to be frank – there are not a lot," he says. "The feds thinks this will give them some level of confidence, some level of interest and predictability to invest in their own country."

But until there is clarity on the bank's remit, we will all be left wondering what its impact will be.

Richard Lee, managing director for project finance and infra at Manulife, says: "I – like many people – still do not know the model that the infrastructure bank will be following. There is a great deal of uncertainty surrounding what this bank is going to do and how it is going to do it.

"Is it going to crowd out other lenders? Is it going to turn into another level of bureaucracy? Or is it going to do what the government hopes it is going to do – which is to leverage private capital in a manner that the government hopes the bank will do."

Political uncertainty…

And then there's the bugbear of political uncertainty. The single most important thing that you can have with any market for the longevity of a PPP programme has to be cross-party consensus.

Without it – and Ontario is not quite there – elections can prove to be the turning point where the incoming party puts everything on hold to re-brand it so they take credit for any future projects that close… or bin the lot, insisting it is the creation of the devil.

Tim Murphy, partner at McMillan – who had the good grace to mention that he is co-chair of Ontario Premier Kathleen Wynne's re-election campaign – reckons the real fork in the road that the province faces is the next election, which is being staged in June 2018.

"Ontario has benefited from the same political party governing it since 2003 as well as consensus on this procurement methodology and the success of this tool for infrastructure assets and services," says Murphy.

"There is an election in less than a year from now and there is more uncertainty than there has been for while over what the outcome will be. For me, the biggest fork in the road is if there is a change of government in the next 10 months.

"The current government – with two successive premiers from the same party [Dalton McGuinty and now Wynne] – have bet a lot of money on infrastructure as an important economic tool. But who knows what is going to happen in 10 months' time?"

As with all markets with a looming election, you can expect to see two political manoeuvres:

- projects accelerated through the procurement process in a bid to get them over the line just before the election – a cheeky vote-winner and feel-good factor
- or drive them on to such an advanced stage that to scrap them after the election would be toxic for the incoming party should the incumbent lose

It is not certain that the new premier – should the Liberals and Kathleen Wynne be ousted – would walk away from the programme, but until there is certainty… doubts will remain.

"When you look back on the track record of investment, there has been a massive amount of money invested in this space," says Murphy. "And, yes, there are only so many schools, hospitals and jails you can build – but what you have seen an uptick in the size of these and a reduction in the number… but continuing support for the model."

Shipshape and Bristol fashion

So it's all looking pretty good for Ontario, then.

All that's left is:

- a smattering of increasingly exotic projects and a procurement model that is not so well suited to their delivery
- an infrastructure bank that is shrouded in mystery
- political uncertainty with an election looming in June 2018

Goodness – that's an unholy trinity.

But for all that, we know… Ontario will retain its poster child status. It has to. You're all we've got.