



## Public investments and public-privat partnerships development

### *Investițiile publice și dezvoltarea parteneriatelor public-privat*

*Associate Professor Angela SECRIERU, Ph.D.*

The Academy of Economic Studies of Moldova, Republic of Moldova  
e-mail: angelasecrieru@yahoo.com

*Associate Professor Viorica LOPOTENCO, Ph.D.*

The Academy of Economic Studies of Moldova, Republic of Moldova

*Eugenia CIUMAC, Ph.D. student*

The Academy of Economic Studies of Moldova, Republic of Moldova

#### **Abstract**

*Countries seeking to build up their infrastructure in different sectors have several options, including raising financing for public investment by borrowing, increasing public saving, and reallocating public spending from other sectors; getting more out of their investments by improving investment planning and project evaluation and implementation procedures; and encouraging private sector investment. The appropriate strategy will vary from country to country, depending on a country's fiscal position. An increasing number of countries have entered into PPPs to promote the private sector supply of infrastructure assets and infrastructure based services.*

**Keywords:** *public-private partnerships, infrastructures, investments, public sector, private sector*

#### **Rezumat**

*Pentru a-și dezvolta infrastructura în diferite sectoare, țările au câteva opțiuni, inclusiv creșterea finanțării pentru investițiile publice prin împrumuturi, creșterea economiilor publice și realocarea cheltuielilor publice de la alte sectoare, creșterea performanțelor investiționale prin îmbunătățirea procedurilor de planificare, evaluare și implementare a proiectelor investiționale și încurajarea investițiilor private. Strategia potrivită va fi diferită de la țară la țară funcție de poziția fiscală a țării. Un număr tot mai mare de țări au dezvoltat parteneriate public-privat pentru a promova oferta privată de active de infrastructură și servicii aferente.*

**Cuvinte-cheie:** *parteneriat public-privat, infrastructură, investiții, sector public, sector privat*

**JEL Classification:** H43, H54

Theoretical substantiation of the *public-private partnership* concept takes its origin in the theory on *X-efficiency* developed by *Leibenstein* in 1966. The idea of this theory consists in that public institutions or enterprises cannot go into bankruptcy, until financial and monetary policies are expansive sufficiently to guarantee survival or to limit probability of their going into bankruptcy. Inefficiencies in the activity of public enterprises or institutions, results from distortional interventions both of government and of the state organizational structures, which are featured usually by a high level of bureaucracy.

Consequently, under this theory, public-private partnerships are necessary in order to reduce sources of X-efficiency in public organizations and to permit them to confront market force and to become more competitive. At the beginning of 80's of the previous century, inefficiencies of public organizations have lead to appearance of so-called *New Public Management* in the United Kingdom of Great Britain and other countries with Anglo-Saxon traditions in their majority. Introduction of operation principles of private companies in public administrations in implicit manner was the main purpose of this innovation.

Below, factors advantaging or disadvantaging PPPs are examined and some hypotheses of it for the event of the Republic of Moldova are stipulated.

Arrangements of PPPs nature permits also to be considered projects that would be impossible to implement in other conditions. In this sense, PPPs assists in coverage of so-called difference between what governments can permit and what citizens require. Thus, PPPs permits public sector to attract more financial resources through involvement of private sector in capacity of an intermediary (Kopp, 1997). Theory suggests that countries encountering with insufficiency of the external sources of revenues (help and assistance, revenues from natural resources, income from petrol, etc.) have undergone severe fiscal crises with following appearance of some parliamentary majority striving to be more opened toward foreign private investments. Due to their specificity, countries with larger external or exogenous resources have undergone economic crises of medium intensity and are less inclined to adopt market-oriented policies (Glasser, 2002) This argument makes viable consideration that countries-renters, which obtain high volume of exogenous income, can attenuate fiscal shocks and, hence, it is less probable that they will promote reforms, liberalizations and participation in arrangements of PPPs nature.

Ethnically fragmented countries require larger number of infrastructural projects or ones with regard to public goods and services. Usually, it is required to respond various individual preferences that prevent association of resources for funding common public projects (Alesina, Baqir, and Easterly, 1999). Thus, with certain level of the government responsibility, various projects satisfy every ethnic group separately and reduce probability of conflicts associated with common resources or goods and services. However, larger number of infrastructural projects causes, as a rule, supplementary financial pressure on the public sector and requires private funding. As it is mentioned above, it is possible to expect that governments loyal to the market-oriented policies are relatively more opened to private involvement in the public infrastructural projects.

While governments try to increase limited resources through private participation in PPPs, private companies are governed by reasons related with obtaining of profits. Thus, profitability of PPPs projects is crucial for attraction of partners from private sector. In general, infrastructural projects are related with high costs and frequently require a certain time for revenues to be generated. This means that commercial risk of such projects is quite

high. Thus, it is possible to anticipate that market conditions affect impetuses of private companies to participate in any infrastructural PPPs. This presupposes that demand for services to be provided and market size is powerful determinants for participation of private sector in PPPs. Infrastructural services provided to large number of consumers paying market price could be more profitable, in general, and permit quicker coverage of non-reimbursable costs. In addition, income level or buying power of potential clients is also important, since it indicates their ability to pay the market prices for services.

As for any investments, aggregate demand at prices dominating at the market can appear to be not strong and intense enough to ensure long-term profitability or it can be the subject of macro-economic shocks. These risks are especially severe in cases when no infrastructural supplier has existed previously, when potential demand is not recognized and when tariffs for public services in the past were subsidized, while their collection was weak. In some arrangements of PPPs type, governments accept responsibility for tariff collection or come to an agreement to purchase infrastructural services from PPPs projects at predetermined prices. Although this reduces risks for private investors, it also requires frequent renegotiations, especially during crisis the periods when governments cannot allow themselves to undertake conditioned obligations or private investors cannot respect contractual provisions (Ehrhardt and Irwin, 2004).

Standard argument for attraction of private investments consists in establishment of stable macro-economic conditions, adequate tariff regimes and reasonable economic policies.

Governments that manage to achieve correct equilibrium reflected, for example, by ratings of the state indebtedness, evaluated by various rating agencies, are adapted better to attraction of private investments and efficient suppliers of infrastructural services. Concurrently with improvement of the country's ratings and macro-economic conditions, governments are able to attract more successfully the suppliers and larger funding (Dailami and Klein, 1997).

Risk of the exchange rate is another variable influencing impetuses of private sector to be involved in arrangements of PPPs nature.

Besides macro-economic stability, institutional quality, due to its direct influence upon country's risk, has an importance for investors. Arrangements of PPPs type represents by definition contractual arrangements. Sustainability of these arrangements as contractual ones depends critically on the regulating environment, which, in its turn, is determined by the quality of institutions. Weak institutions generate incertitude with regard to the quality of regulations with resulting growth of the country's risk. High country's risk decreases impetuses for investors to associate in PPPs. Thus, solid institutions and real supremacy of law is important for security of the PPPs arrangements. Some authors (Pistor, Raiser, and Gelfer, 2000) argue that efficiency of legal institutions has much stronger impact on the availability of external funds than accounting laws.

PPP's are influenced also by the government's reputation and experience of private sector in infrastructural projects of PPPs type. By the reason of specific characteristics of investments into an infrastructure, past experience in management of these projects is a crucial factor for the success of future arrangements. Thus, government's reputation in respecting of previous PPP's is important for attraction of future PPP's.

Further on, action and validity of these PPPs determinants will be evaluated for the case of the Republic of Moldova with results presented in Table 1.

**Action and validity of the factors of PPPs development for the case  
 of the Republic of Moldova**

**Table 1**

	<i>Validity for the Republic of Moldova</i>
<i>Hypothesis 1:</i> It is possible for governments with large budgetary deficit and heavy burden of public indebtedness to have PPPs.	Hypothesis 1 imposes PPPs constitution in the Republic of Moldova
<i>Hypothesis 2:</i> States-renters with large sources of external revenues have weak budgetary constraints and, therefore, are less motivated to participate in PPPs projects.	It is not the case of the Republic of Moldova
<i>Hypothesis 3:</i> It is possible for arrangements of PPPs nature to be correlated positively with ethnic fragmentation.	In the context of hypothesis 3, PPPs constitution in the Republic of Moldova is welcomed
<i>Hypothesis 4:</i> It is possible for government being loyal to policies oriented toward development of the market relations to be involved in PPPs.	Validity of the hypothesis 4 can promote PPPs development in the Republic of Moldova
<i>Hypothesis 5:</i> PPPs is more widespread in countries being stable from the political point of view and having responsible government.	For PPPs development in the Republic of Moldova, political stability and a responsible government shall be implemented.
<i>Hypothesis 6:</i> PPPs is inclined to be more widespread at larger markets with larger demand and buying power.	Hypothesis 6 supposes severe constraints for PPPs promotion in the Republic of Moldova. RM economic integration and funding from other areas and states shall be accelerated.
<i>Hypothesis 7:</i> PPPs is more widespread in countries with credible, predictable and stable macro-economic conditions. In particular, countries with decreased inflation and stable exchange rate are more attractive candidates for PPPs.	See Hypothesis 5
<i>Hypothesis 8:</i> Countries with weak and bureaucratic institutions of low quality can represent increased country's risk and, therefore, it is less probable that they will promote PPPs development.	See Hypothesis 5
<i>Hypothesis 9:</i> PPPs can be more widespread in countries with strong and efficient legal institutions.	See Hypothesis 5
<i>Hypothesis 10:</i> PPPs can be widespread in environments where legal codes protect better investors' rights.	See Hypothesis 5; real protection of investors' rights shall be ensured
<i>Hypothesis 11:</i> Probably, PPPs arrangements are more extended in countries with traditions in PPPs activity.	Hypothesis 11 supposes limits in the PPPs development in the Republic of Moldova
<i>Hypothesis 12:</i> Probably, the share of private participation in PPPs arrangements correlates positively with the degree of mixture of goods and services to be supplied and technological structure required for them in order to be produced and provided.	Valid for PPPs of any type and for any country

Until now, there is only one arrangement of the PPPs type in the Republic of Moldova with participation of the Austrian Concern „EPA MEDIA” – contract on the public-private partnership concluded with the Mayorality of Chisinau municipality on January 19, 2006. Investment project provides designing and construction of station for passengers waiting for public transport, their linkage with European norms, technologies and standards, unification of the urban architectural style of publicity boards and attribution of the modern aspect to outdoor advertising in city. Offer presented by the CFC (Company with Foreign Capital) „Epa Media” Ltd., subsidiary of the Austrian Concern, resident of RM, established under requirement of the Mayorality of Chisinau municipality, provides implementation of the following:

A. *municipal program*: (i) provision of complete funding of costs for designing, construction and maintenance of 300 glass waiting stations for urban public transport corresponding with European and local technological standards; (ii) construction of an unified system of the urban illumination equipment on the basis of double function system – advertising plus illumination source – alongside one of thoroughfares of Chisinau municipality;

B. *social program*: (i) reduction of costs for municipal budget due to the fact that investor defrays expenses for illumination of urban public transport waiting stations, publicity cassettes and advertising luminous equipment destined for community for the period of 10 years; (ii) engagement of the domestic labor force for construction and maintenance of all contractual units; (iii) start-up of the „Today Moldova” program that will promote image of the Republic of Moldova and Chisinau municipality in EU.

C. *cultural program*: support of cultural events and ones of public interest in Chisinau municipality, as well as their promotion in EU.

Total scheduled investment of the CFC “Epa Media” Ltd. for the period of 2007-2016 amounts approximately to 8 million EURO with 6 million EURO to be invested during the period of 2007-2009 (Table 2).

#### Flows of capital generated by PPPs

**Table 2**

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Total
Gross profit	-392680	1046992	2751382	4978294,3	5563428,8	5836556,6	5748987,3	5656061	5566942,1	5467711,3	
Investments	3200000	1755000	1217000	1020000,0	225000,0	125000,0	125000,0	125000,0	125000,0	125000,0	8042000
Purchase costs	1000000	0	0	0	0	0	0	0	0	0	0
Total of capital flow	4592680	5300688	3766306	191988,3	5530417,1	11241973,7	16865961	22397022	27838964,1	33181675,4	

In its turn, the Mayorality of Chisinau municipality permits CFC „Epa Media” Ltd. location and operation of a certain number of advertising supports at the territory of Chisinau municipality.

The main advantage of the Project consists in provision of its integral funding from the part of investor. In addition, if revenues in the municipal budget for 2005-2006 from the tax for advertising placement collected from all advertising agencies in Chisinau municipality amounted to 970.0 and 1645.3 thou. Lei, respectively, the Mayorality of Chisinau municipality will benefit in the result of the project implementation direct

investments in construction of waiting stations for the urban public transport in amount of 34 million Lei with increasing also of taxes collected for advertising placement. At the same time, as an indirect advantage of these PPPs, increasing of revenues in the municipal budget from taxes and duties paid by the domestic economic agents involved in the project implementation shall be noted.

### References

- Alesina, A., Baqir, R., and Easterly, W. (1999). Public Goods and Ethnic Divisions, *Quarterly Journal of Economics*, Vol. 114, No. 4 (November), 1243–1284.
- Dailami, M., and Klein, M. (1997). *Government Support to Private Infrastructure Projects in Emerging Markets*, Policy Research Working Paper, No. 1688 (Washington: World Bank).
- Cicea, C., Vasilescu I. (2004). *Results, the main factor for increasing the efficiency of the public sector*, International Symposium „Alternative Economic Strategies”, URSA Gheorghe Cristea, Era Publishing House, ISBN 973-8153-61-1
- Glasser, B. (2002). *Economic Development and Political Reform: The Impact of External Capital on the Middle East*, Cheltenham: Edward Elgar Publishing.
- Kopp, J. Ch. (1997). *Private Capital for Public Works: Designing the Next-Generation Franchise for Public-Private Partnerships in Transportation Infrastructure*, Master's Thesis; Boston: Department of Civil Engineering, Northwestern University.
- Pistor, K., Raiser, M., and Gelfer, S. (2000). Law and Finance in Transition Economies. *Economics of Transition*, Vol. 8, No. 2, pp. 325–68.