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Government Guarantees in Infrastructure Projects: A Second, Third Look at the Policy

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Introduction

Government guarantee has been used to encourage private sector participation in public infrastructure projects. It is an instrument used to minimize, and in some cases, eliminate the risks that discourage private sector participation in financing, building, maintaining and operating public infrastructure projects. For example, a government credit guarantee can motivate private sector lending for infrastructure projects by mitigating those risks that the private sector cannot evaluate or will not bear.[1] For the past six years, the Philippine government has used government guarantees to encourage private sector participation in public infrastructure projects. A government guarantee is an important feature of the Build-Operate-Transfer schemes that have helped solve the country's power crisis in the early part of the 1990s.

The provision of guarantee, however, is not without cost to the government. It creates a contingent liability which will require careful monitoring, accounting and provisioning in the national government budget to meet future guarantee calls. A contingent liability implies that the payment of claims against the guarantee is conditional on some future event.[2] A guarantee claim for payment will translate into a payment burden on the part of government and thus, from the fiscal management viewpoint, the government must be adequately prepared to meet those contingent liabilities when they become due.

This *Policy Notes* issue argues that the government must move toward project financing structures which will minimize the provision of direct and indirect subsidies, guarantees and equity to infrastructure projects. Given the accessibility of international capital markets arising from the strong economic performance, continuing reform effort and increased confidence of the private sector to risk its capital in infrastructure projects, future project financing structures must decrease government exposure and increase private sector participation in public infrastructure projects. This will require, among

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[1] *See Mody and Patro (1996).*

[2] Ibid.

others, a greater private sector share of the risks of project financing, putting the appropriate price on government guarantees, programming the guarantee resources that will be made available to those projects and allocating them efficiently. Last, but not least, is the requirement to monitor and have an adequate provisioning for the contingent liabilities arising from the grant of government guarantee.

This *Notes* has four parts. Section II briefly presents the Philippine experience with government guarantees to Build-Operate-Transfer (BOT) projects. Section III points out the fiscal implications of the government guarantees. Section IV discusses risk-sharing with the private sector. The last section draws attention to certain points which may inform public policy on the provision of guarantees.

The Philippine Experience with Government Guarantees to BOT Projects[3]

Build-Operate-Transfer (BOT) schemes. The government sought to improve the regulatory and administrative framework for implementing infrastructure projects. Thus, in 1990, Congress enacted Republic Act (RA) No. 6957 (later amended by RA No. 7718 in 1994), more popularly known as the "BOT Law," which allows the private sector to finance, construct, maintain and operate public infrastructure projects. The objectives were to minimize the burden of infrastructure projects on the national government budget, minimize external borrowing for infrastructure projects, and use the efficiency of the private sector in delivering a public good. The BOT scheme is a contractual arrangement between the government and the private contractor which obligates the latter to finance and construct an infrastructure project for the government, and operate and maintain the facility for a definite period of time. During this operating period, the contractor can charge rent, user charges, and toll fees to recover his investment outlay and generate a reasonable return to investment. It is important to note that the private sector brings not only financing for the project but also cost efficiencies together with operating know-how and technical advantage.[4] Thus, the government used the BOT schemes to address the power crisis and more recently, to move other infrastructure such as the Manila Skyway Project, EDSA MRT III and others, from the drawing tables to the project implementation stage.

Private power generation. The government has privatized power generation to provide greater efficiency in the power sector after the government realized the inadequacies of state provision of power and the regulatory and clearance procedures in that sector. The first successful project was the 200 megawatt (MW) Hopewell Navotas I which began operation and was synchronized with the National Power Corporation (NPC) grid in 1991. BOT arrangements were extensively used by the Ramos government to lick the power crisis, believing that private sector participation was the best way to increase power generation capacity in the shortest possible time. The government and NPC launched a "fast track" program with some 10 suppliers for additional power generation capacity of about 1000 MW within 18 months. By the end of 1993, the power crisis was history after the private sector responded positively to its new-found role. Between 1992 and mid-1994, the government and NPC had about 24 more BOT arrangements.

Initially, the arrangements were done on a transaction by transaction basis with individual project sponsors because of the urgency of the situation and the lack of experience with BOT schemes in the country. The resultant agreements were generally on a cost plus or a minimum rate of return basis. However, as the economy recovered and private capital regained confidence in the

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[3]*This section relates the Philippine experience with providing guarantee to BOT projects in the power sector. After the successful private sector-government cooperation in the power sector projects, other infrastructure projects followed suit.*

[4]*Private power projects were completed at lower costs and used 25% to 30% less time than public projects. In Argentina, Chile, Malaysia and Macau, private concessionaires of water supply projects have reduced unaccounted water from 50% to 60% of the total to 15% to 25% and staffing costs by 30% to 50% (Kohli 1995).*

country, the more recent contracts have been awarded on a competitive basis. As of 1994, more than 35 power plants accounting for some 5,000 MW are either already in production or under active development/construction with a total cost of US$5 billion. Except for hydro and geothermal power, all future power generation capacity will be with the private sector.[5] Table 1 shows the available information on the different power projects in the Philippines and their comparative costs.

Because the power crisis was the single most important factor to economic recovery and growth in the early 1990s, the government accepted the installation of "peak-load" power plants that provided the much needed power but at a relatively higher cost to the consumer. But after the power crisis eased up, the government sought less expensive power projects.

The benchmark price for private power in Luzon island grid has dropped steadily from US$0.085 per kilowatt hour (kwh) under the "fast track" power program to less than US$0.05 per kwh in the more recent BOT arrangements where contracts were awarded after com-

[5]*This paragraph draws on an unpublished World Bank document on power development in the Philippines.*

Table 1. Cost of Private Power Projects

Project Name	*Contractor*	*Type*	*Capacity MW*	*Fuel*	*Year Operation*	*Est. Cost US$ Mn*	*Cost US$/kW*
Navotas GT 1-3	Hopewell Holding-HK	BOT	210	Diesel	1991	41	195
Subic, Zambales Diesel I	Enron Power Co. - USA	ROL	108	Bunker	1993	135	1250
Navotas GT 4	Hopewell Energy Int.-HK	BOT	100	Diesel	1993	40	400
Limay-Bataan CC GT "A"	ABB/Marubeni/Kawasaki	BTO	300	Diesel	1993	330	1100
Makban Binary Geothermal	Ormat Inc.-USA	BTO	15.73	Geothermal	1993	17	1049
Pinamucan, Batangas Diesel	Enron Power Co.-Inc.	BOT	105	Bunker	1993	120	1143
Calaca Batangas Barges	Far East Levingston	BOO	90	Bunker	1993	78	867
Limay, Bataan CC "B"	ABB/Marubeni/Kawasaki	BTO	300	Mix	1993	350	1167
Bataan EPZA Diesel	Edison Global (HK)	BOO	58	Bunker	1994	31	534
Cavite EPZA Diesel	Magellan Utilities	BOO	63	Bunker	1994	22	349
Bacman Geothermal	Ormat Inc.-USA	BTO	15.73	Geothermal	1994	17	1049
Malaya Skid-Mounted Diesel	Pro-Tech	OL	50	Bunker	1994	14	280
Eng'g. Island Barge	Sabah Shipyard Sdn BHD	BOO	100	Naphtha	1994	30	300
Bauang, La Union Diesel	First Private Power-PHIL	BOT	215	Bunker	1994	285	1326
Pagbilao, Quezon Coal I	Hopewell Energy Int.-HK	BOT	350	Coal	1995	491	1401
Pagbilao, Quezon Coal II	Hopewell Energy Int.-HK	BOT	350	Coal	1996	491	1401
Tongonan Leyte-Luzon	PNOC-EDC/Private	BOO/BOT	440	Geothermal	1997	486	1104
Sual Pangasinan Coal	Hopewell Holdinh (HK)	BOT	1000	Coal	1999	1100	1100
Toledo Cebu Coal	Atlas Consolidated-PHIL	ECA	55	Coal	1993	60	1091
Iligan Diesel I/II	Alson/Tomen -PHIL/Japan	BOT	98	Bunker	1993	60	612
TOTAL			4023			4196	1043

Source: World Bank.

petitive bids. Table 2 shows the prices and costs of independent power producers (IPPs) for Base Load Generation. Those power plants in 1994 onward provide electricity at a lower cost than that provided by power plants of the "fast track" period.

During the "fast track"period of installing more power capacity through the BOT schemes, the independent power producers required comprehensive government guarantees. These covered sovereign, foreign exchange convertibility, market and credit risks. Comprehensive guarantee coverage was required because government's ability to finance and install in the shortest possible time the much needed power generation capability was inadequate and because the country had very limited access to private risk capital. Thus, government had no other choice but to provide all the required guarantees, including guarantees for NPC's obligations, "take or pay" undertakings backed by a sovereign guarantee. Ideally, the government should have provided guarantees only to "fundamental" risks or those pertaining to sovereign and political risks.

Table 2. Philippine Prices and Cost of IPPs for Base Load Generation (in USc/kWh)

	Financial Prices		*Economic Costs*	
	Average	*Sensitivity Range*	*Average*	*Sensitivity Range*
By Technology				
Diesel	5.64	5.24- 7.66	5.34	4.95-7.23
Gas Turbines	9.01	8.93-13.05	6.15	6.10-9.85
Steam-Coal	6.19	5.69- 7.35	5.03	4.61-5.85
Comb'd Cycle	5.96	5.56- 6.27	5.35	4.65-6.05
By Commissioning Period				
1991-1993	6.87	5.24-13.05	5.91	5.22-9.85
1994 onward	6.04	5.39- 7.35	5.21	4.61-5.93
TOTAL	*6.52*		*5.62*	

Source: World Bank.

However, recent BOT projects indicate the country's progress in attaining an improved credit standing in the international capital markets which has enabled government to provide a less comprehensive risk coverage. This is seen in BOT arrangements in toll road construction and in urban mass transit system. Thus, the success of the BOT arrangements has encouraged government to pursue greater private-public sector collaboration in several areas:

- privatization of the power sector which will involve the sale of NPC's generating assets and the geothermal resources of the PNOC-EDC in the future, including possible privatization of transmission;
- deregulation of the energy sector which was preceded by the 1994 privatization of Petron, a government oil refining and distribution company;
- bidding out of water distribution and sewerage operation;
- extending BOT arrangements into other public utilities such as toll roads, rail transport and developing Subic and Clark, former US military bases, into important regional industrial zones.

Tollways construction.[6] The project was the construction of a 25.5 kilometer toll road costing US$500 million connecting Metro Manila to the Calabarzon development area in Cavite province. Through a bidding process, the government awarded a 35-year BOT concession to a joint venture between a private sector consor-

[6]*Drawn from the speech of Secretary of Finance, Roberto de Ocampo, in the High Level Conference on Frontiers of the Public-Private Interface in East Asia's Infrastructure, Jakarta, Indonesia, September 3, 1996.*

tium and the government's Public Estates Authority. The government's guarantee cover was limited to political and sovereign risks, including right of way, force majeure during construction and operation, and cost escalation arising from variations in design. A novel idea introduced was the guarantee on the parametric adjustment of toll rates. This means that government guarantees the proponents compensation for any shortfall in toll revenues arising from the non-implementation of an agreed-upon parametric adjustment of toll rates. While the government took the tariff risks, all other commercial and market risks, e.g., the volume of traffic that will actually use the toll road, were absorbed by the private investors and lenders.

Light railway system.[7] This involves the construction of a 17-kilometer light railway system traversing Epifanio delos Santos Avenue (EDSA). The US$650 million project was awarded to the private sector on a 25-year "build-lease-transfer" arrangement. The original plan was to finance the project from commercial borrowing from foreign capital markets with the government providing only fundamental guarantees. However, government, through the Department of Transportation and Communication (DOTC) and the Department of Finance (DOF), took the initiative of helping the private sector consortium negotiate for lower financing costs with the senior lenders of the projects. The government guaranteed the lease payments of DOTC to the proponents with confirmation from DOF that the obligations carry the full faith and credit of the Republic of the Philippines. With this performance undertaking, the interest rate to investors was brought down from 20 percent to 15 percent. The project was also made more commercially attractive to the private sector consortium by awarding them the right to commercial development in the depot and stations for which they would have to pay lease to the government. Thus, the fare revenues will be supplemented by revenues from commercial developments.

Independent power project.[8] For a proposed 1,200 MW independent power project, the government will provide cover for

- fundamental risks composed of political and sovereign risks,
- foreign exchange convertibility risks, and
- project specific risks.

An innovation is the inclusion of provision for a "fade away" or "sunset" of the guarantee cover for the last two types of risks subject to the Philippines attaining investment grade status in the international capital markets. The proponents have the option to retain the guarantees by paying the corresponding guarantee fees. To arrive at the private sector valuation of the guarantee cover, the government has asked proponents to submit bids "with" and "without" guarantee cover.

Emerging framework for providing guarantees. The Philippine experience shows how the nature and extent of government guarantee evolves over time as the economy strengthens and private sector profitability is enhanced. From the full comprehensive guarantee cover during the early days of the power crisis, the government is now sharing the risks with the private sector. More specifically, commercial and market risks that appropriately belong to the private sector are no longer covered by government guarantee. The government has also unbundled the risks it is willing to cover into three types of risks:

- ***Fundamental risks*** consisting of sovereign and political risks such as expropriation by government, nationalization, changes in law and force majeure for which the guarantee is given free.

- ***Foreign exchange convertibility risks*** for which a corresponding guarantee fee will be paid. The guarantee "fades away" once the country is rated investment grade by international credit rating agencies for two consecutive years. An option to continue with the guarantee is given provided the guarantee fees are paid.

[7]Ibid.

[8]Ibid.

❊ ***Project specific risks*** where the guarantee will be limited to the senior lender and for the original term of the loan excluding returns to equity holders. Guarantee is provided for right of way, peaceful (project) site occupancy and other related concerns. The guarantees are priced with a "fade away" provision based on the rating of the corporation implementing the project but with an option to extend the guarantee cover upon payment of the corresponding fees.

In the beginning of the private-public cooperation in infrastructure projects, project approvals and provision of government guarantees were undertaken without the benefit of a clear statement of policy, legal and regulatory framework. The Philippine experience illustrates the need to clarify this framework and the government's commitments, establish the payment process for guarantee calls, and seek support arrangements from export credit agencies.[9] The enactment of the BOT Law and its subsequent amendment was a very critical input toward clarifying objectives and delineating private-public sector responsibilities.

With respect to the regulatory framework, the government is strengthening regulatory institutions through long-term training. More importantly, to encourage efficiencies and fair pricing, the government is pursuing sectoral reforms and is putting in place rules and conditions that foster competition. As earlier stated, the initial BOT arrangements were done on a transaction by transaction basis without the benefit of open competition. As the government gains experience in BOT arrangements and the provision of required guarantees and as the economy recovers, the stage has been set for competitive bids in infrastructure projects. This will ensure transparency and reduce transaction costs.[10]

It is important to introduce policy and institutional reforms to various sectors, e.g., water, information technology, energy, to attract sustainable private investments. The country's power generation objectives were achieved largely because of the government's decision to deregulate power generation. The efficiencies brought about by the reforms will enable the private investors and lenders to bear the commercial risks (which they should bear in the first place) and get a reasonable return on their investments. Financial sector reforms should continue in order to encourage long-term risk capital in the financial markets and innovative and better-priced financial products.[11]

Net Fiscal Impact of Government Guarantee Exposure

This section presents the net fiscal impact as the difference between the lower demand for public sector resources because of the availability of private sector resources and the stock of contingent liabilities created by the government's guarantee exposure. The BOT arrangements have enabled the government to avoid new indebtedness and an increase in public sector deficits but the government guarantees provided to those BOT infrastructure projects have also given rise to huge contingent liabilities.

Available figures show that in 1992, investments in BOT projects amounted to as much as P12.8 billion or 0.9 percent of GNP. In 1995, these investments rose to P51.4 billion or 2.6 percent of GNP. These amounts would have been borrowed by the government and they would have increased interest rates on average by 2.1 percentage points and inflation by some 4 percentage points

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[9] *OECD countries' export credit agencies provide guarantees against risk of nonrepayment to their national exporters or banks which lend to overseas importers of goods and services. During the period 1983-91, export credit agencies had US$53.1 billion worth of business with a maturity period of 5 years or more. Of this, 60% were for infrastructure finance linked principally to the import of capital goods (1994 World Development Report).*

[10] *The government may have to provide an* a priori *announcement of the form and level of government support arrangements and seek the best market offer from proponents.*

[11] *See Lamberte and Llanto (1995) for a lengthy discussion of financial sector policy and institutional reforms.*

between 1992 and 1995.[12] The government provided guarantees to the BOT projects. The estimated cumulative guarantee payments to BOT operators amount to US$89.4 billion over the period 1994 to 2019. Assuming a 15 percent discount rate, the net present value of the guarantees to BOT projects has been put at about P208.3 billion or 10.6 percent of GNP in 1995.[13] However, the government does not expect any widespread call on the government's guarantee in the near future. Thus, assuming a guarantee call of 3.8 percent of outstanding guarantee cover, the government is expected to pay out some P4.4 billion in 1992 to P13.0 billion in 2000. Annually, the average is about 0.3 to 0.4 percent of GNP. Notwithstanding the imperfections in the estimates, *the point the paper stresses is that guarantees generate contingent liabilities which must be managed well. Otherwise, the government will be exposed to huge payment burdens once a guarantee call is triggered*.

This brings us to a number of issues that the government must work on. They are: (a) accounting and monitoring of contingent liabilities, and (b) programming and allocation of the government guarantee cover. The overall impression is that there is no comprehensive and detailed accounting and monitoring system for contingent liabilities. In addition, there is no programming and allocation of government guarantee cover.

Governments do not usually account for contingent liabilities because government budgets are typically maintained on a cash basis.[14] A direct government loan is actually recorded as an outflow but the government guarantee is not recorded because nothing has been spent during the accounting period. The cost of the guarantee is accounted for only when a default and the ensuing guarantee payment occur. For fiscal prudence, there is thus a need for a systematic accounting system of contingent liabilities. Canada, the United States and other countries have an accounting system for contingent liabilities. A systematic accounting, monitoring and reporting are important to serve as early warning to the government of potential guarantee calls and the amount of government exposure. A good example of this practice is the requirement under the U.S. Credit Reform Act of 1990 for the budget to reflect the outlays required to cover loan guarantees. Each federal agency that administers credit programs has five accounts: a credit program account, a financing account, a liquidating account, a non-credit account and a receipts account. There are separate financing account for loans and guarantees. In their annual requests for budgets, agencies have to include estimates of the subsidy costs for new loans and guarantees. If an agency exhausts its subsidy appropriations in a given year, it cannot provide further credit assistance in that year.

In addition, there is a need for programming and allocation of the guarantee cover that the government can at any one time afford to provide. Together with monitoring, the programming exercise will provide government useful information on the value of contingent liabilities, allowing it to determine how much guarantee *ex ante* can be reasonably provided without unduly exposing the government to unmanageable liabilities. In this respect, there is a need for a system to rank or prioritize access to the government's guarantee. At the moment, there is no internally consistent programming of guarantee resources, much less provisioning for potential guarantee calls. In the event of a call, the government must have the liquidity to pay the claims of the affected party.

Sharing the Risks with the Private Sector

Public infrastructure projects carry various risks that may discourage private sector financing, construction or operation. Unless the government assumes some or all

[12] *Gil Beltran, in a presentation of the impact of the BOT program on the fiscal sector, Punta Baluarte, Batangas, September 8, 1996. The assumed guarantee call of 3.8% is based on the actual 3.8% subsidy ratio of 14 major nonfinancial GOCCs from 1985 to 1995.*

[13] *Mody and Patro (1996) criticize the use of net present value methods because it is not clear what appropriate discount rate to use and also because the value of the guarantee depends on parameters that change over time.*

[14] *This paragraph is drawn from Mody and Patro (1996).*

of the risks associated with the project, the economy will tend to underprovide it. The underlying rationale of the government's absorption of risks in public infrastructure projects is that the project's social return exceeds its private returns and that society will be better off having the project than doing without it. Thus, a government guarantee is given to project lenders and/or sponsors to minimize the attendant risks of an infrastructure project and thereby, encourage private sector participation.

A practical approach in dealing with this problem of underprovision is to identify and break down the risks associated with the infrastructure project into several components and assign the component risks to the parties that should absorb them. The key activities are

- the optimal assignment of risks to the parties that should absorb them, and
- the minimization of the component risks through efficient risk management.

To encourage private sector participation and performance in public infrastructure projects, the government and the private sector may agree on the assignment of the component risks and the determination of the extent of risk sharing. For instance, the government can guarantee the debt exposure of private sector investors for a limited period of time.

The critical action to take then is to determine which risks are transferable to the private sector and encourage greater private sector share of those risks. The delineation and sharing of component risks are necessary to prevent perverse incentives that lead to project mismanagement,[15] and to avoid moral hazard problems such as relaxing on project monitoring and concentrating on fund diversion. By taking on the full extent of the risk of defaults, the government may end up holding the proverbial empty bag as private lenders and sponsors take strategic action to capture rents at the expense of the government. The satisfactory allocation of risks between the government and the private sector is essential to the successful implementation of infrastructure projects.

Related to this is the need for an explicit exit strategy for government guarantee to minimize the government's risk exposure and contingent liabilities arising from the provision of guarantees. For example, a conscious limitation of the time period or situation under which a guarantee is operational should be considered. This approach minimizes the government's risk exposure and induces government to more efficiently leverage its guarantee cover for infrastructure projects.

The other side of the government's guarantee exposure is the substantial reduction in actual public sector resource requirements for public infrastructure projects. Through the BOT scheme, private sector resources are brought to bear on requirements of infrastructure projects for financing, maintenance and operation. This relieves the government of the need to raise substantial amounts of public monies for the infrastructure projects at hand and allows it to divert public resources to other competing uses. With a relatively low tax revenue effort, the loan markets seem to be the logical source of project finance but this may not be a feasible option if it raises the borrowing costs in the economy. The other option—printing money—is not attractive either because of its potential for creating inflationary expectations.[16]

On balance, the government must compare the impact of lower (present) demands for government resources because of guaranteed BOT projects with the stock of contingent liabilities created by the guarantee

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[15] *Eichengreen (1995) observed that in the late nineteenth century, speculators diverted public sector funds because government-guaranteed loans to the railways were not monitored. Mody and Patro (1996) point out that to create an incentive for continued project monitoring and to filter out lenders who have little ability to manage risk, governments seek to share risks with private lenders by guaranteeing less than the full amount of the loan.*

[16] *The country can ill afford to neglect public infrastructure investments at this time. These fell from 5% of GDP between 1979 and 1983 to less than 2% in the latter part of the 1980s with disastrous impact on the economy, among which is the power deficiency in the early 1990s.*

cover and the potential guarantee calls in the future. A positive net fiscal impact augurs well for government while a negative fiscal position should trigger a review and reorientation of the government's guarantee policy.

Conclusion

The following conclusions may help inform public policy on government guarantees:

❋ ***Importance of a clear and transparent policy framework***. The importance of a clear set of rules, a fairly stable legal and regulatory system in attracting private risk capital cannot be overemphasized. However, there is a need for continuing reforms in the various sectors, e.g., energy, information technology, water, etc. Areas for reform consist of the removal of barriers to entry and competition, public monopolies, and pricing policies, among others. This includes financial sector reforms that will encourage long-term private lending and innovative, better-priced financial products. This also calls for a careful review of the necessity of providing government guarantees in view of the huge stock of contingent liabilities they create. From the policy perspective, government must ask itself whether other avenues to stimulate greater private sector participation have been considered before granting guarantee cover.

❋ ***Strategic value of government guarantees***. The Philippine experience has shown the high value put by the private sector proponents to government guarantees. The power crisis was solved largely because of the government's policy of providing the private sector a greater role in infrastructure projects and of ensuring ample investment protection scheme by way of government guarantees. Thus, the government has a policy tool which it can use to its advantage but not before considering an optimal sharing of risk with the private sector and appreciating the fiscal burden of contingent liabilities.

❋ ***Unbundling and assignment of risks***. Breaking down risks into its components and assigning them to the parties that should bear them are now basic principles motivating the provision of Philippine government guarantee. This approach minimizes moral hazard problems and reduces the contingent liabilities of government. The situation has radically changed from that which forced the government to provide comprehensive guarantee, including market or commercial risks, to that where risks would be shared with the private sector.

For example, in toll roads and rail transport, commercial risks are either being shared, if not being fully borne, by the private sector. In these projects, the government guarantees the implementation of parametric adjustment in toll rates which means that the private proponent will be indemnified if the parametric adjustment is prevented by political pressure or judicial pronouncement.

Thus, the current policy thrust is to limit guarantee cover to those that are appropriately under the responsibility of government, namely:

❋ fundamental guarantees covering sovereign and political risks,

❋ convertibility guarantees covering foreign exchange convertibility risks, and

❋ project-specific guarantees covering problem areas as right of way, tariff schedule, construction, operation and maintenance risks.

❋ ***Exit strategy for guarantees***. Realizing that guarantees need not be permanent features of project financing structures, the government is now considering a "sunset" or "fade away" clause in guarantee agreements. For example, a guarantee on foreign exchange convertibility "fades away" once the country attains investment grade rating in the international capital markets. Having the economy on the path to sustainable growth which provides private investors higher and more predictable returns to investments has certainly strengthened the negotiating stance of the government with private sector lenders and sponsors.

❋ ***Appropriate pricing of government guarantees***. There is a need for an appropriate pricing of guarantees.

For example, in a forthcoming bid for a major power project, the bidders have been requested to provide bids with and without the government's guarantee to obtain a benchmark on the private sector valuation of such guarantees. Pricing is important because the guarantee is not a costless commodity. On the other hand, inappropriate pricing enlarges the exposure of government to contingent liabilities which create potential payment burdens once the guarantee call is triggered.

❄ ***Contingent liability accounting, monitoring, programming and provisioning for the guarantee exposure***. The growth of contingent liabilities creates potential budgetary problems for the government. An appropriate and explicit accounting and budgeting for contingent liabilities must be undertaken by government. Clearly, there is a need to account for the guarantees so far provided and the associated contingent liabilities, monitor them, and undertake a programming exercise to impose budgetary discipline over the allocation of guarantee cover. Appropriate accounting, budgeting, programming and monitoring will result to a more credible guarantee policy, manageable fiscal position and continuing private sector participation in infrastructure projects.

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