



The rise and fall of Public–Private Partnerships in China: a path-dependent approach

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ABSTRACT

Due to growing traffic demand, enormous investment requirements and high fiscal pressures, China has witnessed a reshaping of financing policies in large transport infrastructure projects from public financing to Public–Private Partnerships. As a result, the provision of transport infrastructure services in China has been steadily moving from the realm of government to that of private sector. In the same period, governments at the central and regional levels were actively engaged in this institutional transition by devising corresponding policies and enacting new laws and regulations. However, in late 2009 it became clear to the authors of this article that there has been a tendency of rolling back private participation in transport infrastructure and service because of various forms of opportunistic behavior on the part of some private players and malpractices among some governmental officials in their interaction with private players, and in relatively recent a number of large transport projects have been granted to state-owned enterprises. Therefore, the purpose of this article is to analyze and explain the processes of rise and fall of Public–Private Partnership in China. We argue that the adoption of Public–Private Partnership in China is a path-dependent process rather than some economic optimum advocated by a variety of international organizations. Specifics of wider Chinese political, cultural and institutional context are recognized as important factors that influence the performance of Public–Private Partnership. Effects of decisions made under transitory conditions can persist long after those conditions have vanished. In addition, these historical legacies are important in understanding contemporary use of Public–Private Partnership in China, and they are also the origins from which the sub-optimal statuses are often led.

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1. Introduction

The mass of large transport infrastructure projects and enormous investments that go with it has led to a reshaping of financing policies in the past decades in China. Until recently, one could observe a shift from public-financed projects to a larger share of Public–Private Partnerships (PPPs), which became visible in subway construction (Cong et al., 2007; Zuo and Tang, 2007; Xie and He, 2006; de Jong et al., 2010) as well as in road construction and maintenance (Han, 2009; Chen, 2008; de Jong et al., 2010). After the founding of the People's Republic, the Chinese government adopted a state-centric and top-down approach to infrastructure development, which comprised the entire life-cycle; that is from planning, finance, design, construction, maintenance through operations. Initially, given the nature of network-bound infrastructures as public goods, these arrangements worked reasonably well, especially for the expansion of railway services. However, after decades of low productivity, poor accountability, low efficiency, lack of financial returns and continuous growth in traffic demand, a clear need had grown to improve performance across all sectors

and enlarge the capacity even faster than the already substantial public funds allow for. Confronted with fiscal constraints, the Chinese government then sought to attract private investment to fill the gap. Roughly speaking, from 1993 to 2007 the provision of transport infrastructure services in China has been steadily moving away from the realm of government to that of the private sector through PPPs. From roads to ports, and later to subways, state-owned, monopolistic enterprises gave way to a wide range of private players operating in a relatively competitive environment, accompanied by promising, but far from complete economic regulation (Huang et al., 2009; de Jong et al., 2010). Governments at the central and regional levels were actively engaged in this institutional transition by devising corresponding policy frameworks and enacting new regulations such as independent regulatory agencies (for instance, project tendering committees), competition law and adjusting property rights law.

However, in late 2009 it became clear to the authors of this article during interviews with public officials with the Chinese National Ministry of Transport and regional governments (Shenyang; Dalian; Beijing) that a trend of rolling back private participation in transport infrastructure and service has set in due to harmful forms of opportunistic behavior on the part of some private players as well as malpractices seen among a number of governmental officials in their interactions with private players.

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From about 2007 to 2010, a large majority of new large transport contracts were granted to state-owned enterprises (SOEs). This shift can be largely explained by the fact that many projects granted to private contractors were either abandoned, eventually transferred to SOEs for successful completion or otherwise did not meet expectations. Compared to projects following the conventional approach a lot of effort has been put into (re)negotiations and monitoring deviant behavior by private sector players, thus enhancing transaction costs. Apparently, SOEs began to be perceived as a more reliable and stable solution.

To explain the dissatisfaction with private involvement, it can be argued that the government should first have put into place the institutional framework before relying on PPPs to do the job. For instance, effective legal preconditions such as the application of rule-of-law, transparency law, strict competition law, decent regulatory oversight, smart incentive mechanisms and an effective and efficient judiciary system to some extent are still lacking. Moreover, the relative weakness of the private sector in this area, the absence of substantial numbers of large-scale contractors in parts of the country, the disrespect paid to open tenders and their systematic application and the strong position of SOEs at the capital market and in their personal and organizational networks remind us of the specifics of the wider Chinese political, cultural and institutional context. It shows the importance of considering this as a path-dependent process rather than one heading in the direction of some economic optimum advocated by international organizations such as the OECD, World Bank or IMF. History demonstrably influences the performance of PPPs. Choices made on the basis of transitory conditions can persist long after those conditions have vanished. Understanding contemporary practices requires taking into account past conditions, the choices made in these circumstances and what their legacy means for the current situation and its policy dilemmas. This article will address the question *how the rise and fall of PPP in China can be explained as a path-dependent process*.

By providing answers to the question above, the authors hope to contribute to: (1) the knowledge regarding the status quo of the use of PPPs in China, (2) the Chinese practice in carrying out transport project financing, (3) a hint of how an evolutionary economic perspective can enlighten the understanding of the Chinese historical path of transport infrastructure reforms and its influence on relations between the public and private sectors; and (4) an explanatory framework that puts future policy choices in China in this field in perspective. We have based ourselves on existing literature on PPPs, a touch of policy network theory and evolutionary economics for the appropriate explanatory terminology, leading reports and documents published by various Chinese governments (national, provincial, local) and a number of interviews with policy-makers and experts working for governmental organizations and universities.

In the next section the theoretical concepts and ideas we derived from the literature are presented. Next in Sections 3 and 4 the empirical developments making up the rise and fall of PPPs in China are described respectively. Section 5 interprets these events from an evolutionary perspective, by identifying the unique Chinese path towards the involvement of private parties in transport infrastructure, drawing lessons regarding the Chinese case, and exploring possible further developments, building upon this analysis.

2. Basic explanatory concepts

In this section the concept of Public–Private Partnership and factors that underlie its adoption and success or failure are introduced. Since Public–Private Partnership is an institutional practice that is taken from other settings and transplanted into the Chinese

context, influencing China's development towards a new institutional reality, theoretical concepts and notions from evolutionary economics and institutional transplantation are discussed, in order to select concepts and theoretical ideas that will be helpful in understanding and analyzing the developments regarding PPPs in transport infrastructure in China.

Public–Private Partnerships (PPPs) can be loosely defined as cooperative institutional arrangements between the public and private sectors; they have gained wide interest around the world (Hodge and Greve, 2007). Some see it as a new tool in public management that will replace the traditional method for public service delivery, thus being a revolution in infrastructure provision and project finance (Vincent-Jones, 2000; Mohr, 2004; Shen et al., 2006; Chinyio and Gameson, 2009), while others consider it merely a way to handle infrastructure projects constrained by the availability of funds or technologies absorbing strengths from both the public and the private sectors (United Nations, 1998; Black et al., 2000; Bank, 2004; Maskin and Tirole, 2008). From this perspective, each of the participants must bring something of value to the partnership such as the best available skills, knowledge and resources and transfer them to the arrangement to strive for a “value for money” in the provision of public infrastructure services. Cross-cutting the diverse interpretations, our definition here would be that PPP projects involve private actors in the design, financing, construction, maintenance, operation and management of a public infrastructure on the basis of competitive tendering and long term contracts or arrangements (de Jong et al., 2010). In this process of intermingling public and private sector interests and strengths, a policy network of interdependent actors can be discerned, albeit one often strongly regulated by legal requirements for fair and solid contracting practices (Hodge and Greve, 2007; Klijn and Koppenjan, 2000; Koppenjan, 2005). These actors have different and often conflicting objectives, interests and strategies (Kickert et al., 1997; de Bruijn and ten Heuvelhof, 2008), which leads to difficulties in making a regulatory framework for PPP, applying PPP in specific cases and negotiating among the actors involved in contract formulation.

In analyzing how private enterprises in China are contributing to the partnership and thus to the development of public transport infrastructures, we need to understand how the term “private” is defined and used. Appendix A gives an overview of different types of Chinese enterprises, which contribute different advantages to PPP. For instance, the involvement of private shareholding cooperatives and corporations, as well as foreign-funded enterprises, makes the infrastructure purchasing process more competitive, while state-owned and collectively-owned enterprises are more reliable in terms of capital chain, management, technological and personnel strength for government to contract with. Depending on different options of PPP and thus different responsibility allocation mechanisms in formulating the PPP arrangements, the involved private enterprise may bring different skills and resources to the partnerships. For instance, in the BOT (Build–Operate–Transfer) contract, the private partner contributes the partnership through construction skills, some private capital, operation and maintenance skills and personnel. However, in PPP contracts like TOT (Transfer–Operate–Transfer), the private partners only need to contribute their operation and maintenance skills. In BT (Build–Transfer), private partners are just construction companies with construction skills, but they do not provide capital.

PPP contracts have very important repercussions for all signatories, making the drafting of contracts an often lengthy and costly process. As a result of PPP contracts being incomplete, the possibility of strategic behavior on both sides and possibly high transaction costs due to monitoring efforts and renegotiations remain high (Laffont and Tirole, 1998; Maher, 1997; Dixit, 1996, 2003; Parkera and Hartley, 2003; Williamson, 1996, 2008; Ho, 2009). In PPPs,

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