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Minimum feasible tariff model for BOT water supply projects in Malaysia

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Abstract

A key issue in implementing water supply projects based on the build, operate and transfer approach is risk allocation. Project risks should be allocated to the best competent party through proper contractual arrangements or through government support so as to achieve a low water tariff. The details of tariff design in BOT water supply projects are identified, and a minimum feasible tariff model is proposed for effective risk allocation arrangements. Risk analysis based on a real project in Malaysia is performed to demonstrate the application of the simulation model on the key factors of inflation, exchange rates and demand risk. The analysis shows that for inflation risk, a pre-set tariff adjustment formula is useful in lowering minimum feasible tariff. For exchange rate risk, the reference rate should be set lower than the best estimate. Lowering of minimum feasible tariff can also be achieved if the tariff for additional demand is lower than the tariff for guaranteed demand.

Keywords:

BOT

water supply project

risk allocation

tariff-at-risk

minimum feasible tariff

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