PPP and The Role of Project Finance

John Sachs, Director, Taylor-DeJongh

Public Private Partnership Conference
31 October, 2009

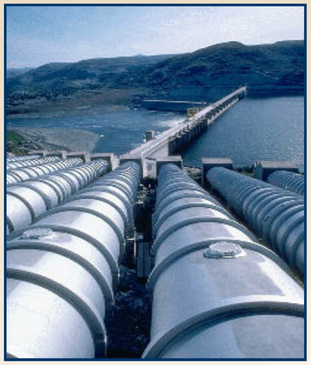
TAYLOR-DEJONGH

TAYLOR-DEJONGH OVERVIEW

- One of the top independent financial advisors and energy M&A firms in the world.
- TDJ ranked as #1 project finance advisor globally for energy sector for 5 of the last 6 years.
- 28+ years of successful transactions in more than 100 countries.
- Aggregate value of financings over **US$70 billion**.
- Offices in Washington, D.C., London and Bahrain.

Industry Focus

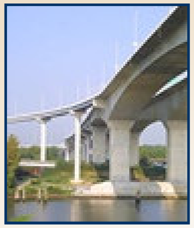
Energy Expertise



- Oil & Gas
- LNG
- Unconventional Oil & Gas
- Petrochemicals

- Conventional & Alternative Power
- Pipelines
- Refineries

Infrastructure & Industrial Expertise



- Industrial, Metals & Mining
- Transportation and Logistics
- Water and Wastewater
- Telecommunications

Closed Deals and Mandates

pfi 2008 League Tables New Mandates

#6 in EMEA
#4 in Asia Pacific
#5 in the Americas

ij league tables 2009 First Half League Tables

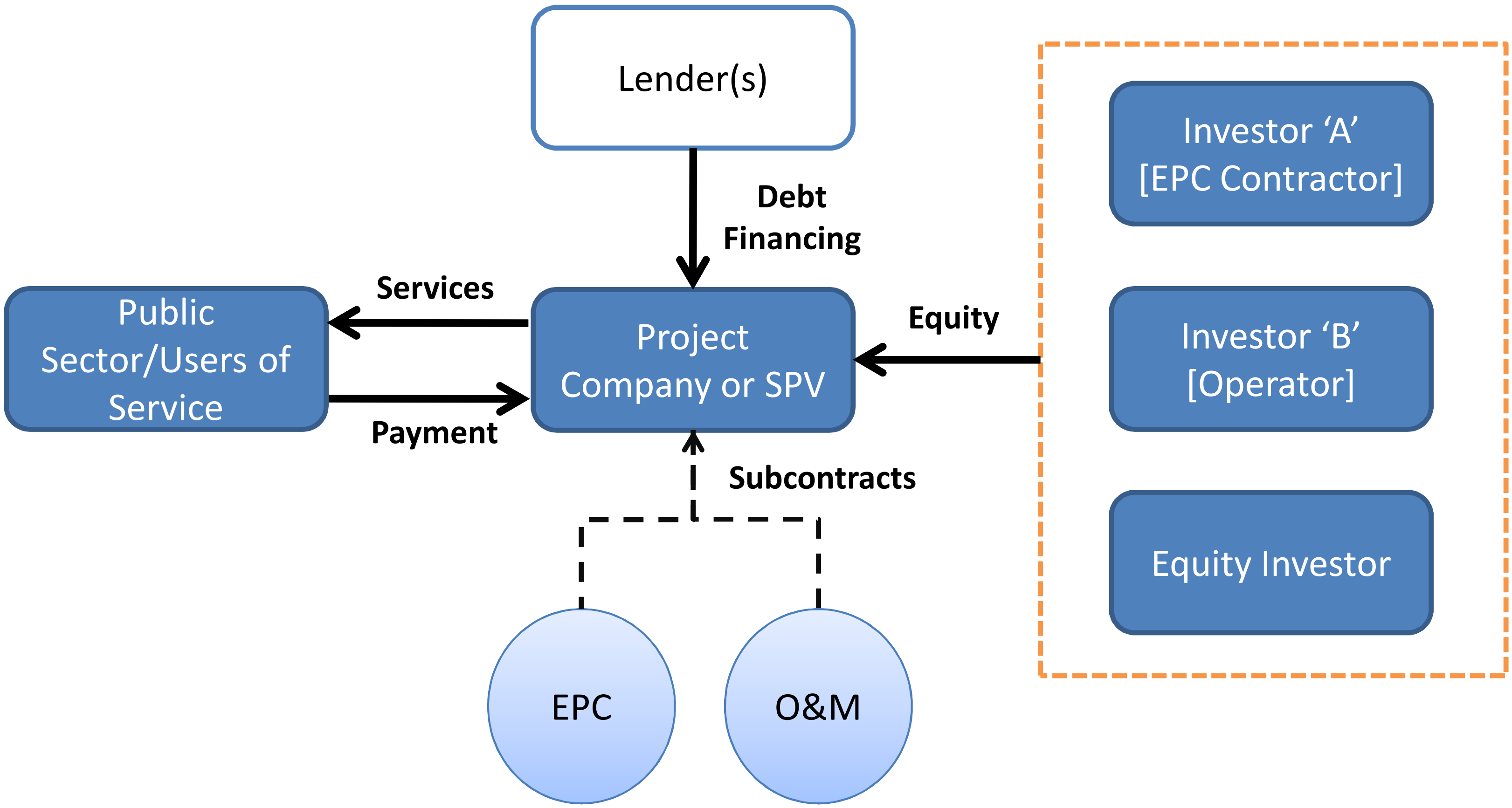
1st Half 2009, Closed Deals
#1 for North America
#7 in Transportation

1st Half 2009, Mandates Won
#4 for Africa and Middle East
#1 in Metals & Mining
#2 in Water and Wastewater
#3 in Renewables

Source: *Infrastructure Journal* 2009 H1 League Tables, as of July 2009 , *Project Finance International* 2008 League Tables, *Dealogic* Global Project Finance Review for First Quarter 2009.

PUBLIC PRIVATE PARTNERSHIPS (PPP) – A TYPICAL STRUCTURE

A PPP is a partnership between the public and private sector, underpinned by a long term contractual agreement. Under the agreement, private sector is involved in the ownership, development, financing, building, and operation of a public facility or service.



FINANCING PPPs: THE ROLE OF PROJECT FINANCE

What is Project Finance?

A debt financing technique suited to capital-intensive projects in which lenders look principally to the cash flows expected to be generated by the project for the repayment of the loan and to the assets of the project as collateral for the loan, rather than to the general credit of the project sponsor.

Why Project Finance?

Governments:

- Have traditionally financed large infrastructure projects but now find it increasingly difficult to fund large investments;
- Are increasingly turning to the private sector to finance, build, operate and maintain a variety of infrastructure services. Seeking efficiencies and value for money.

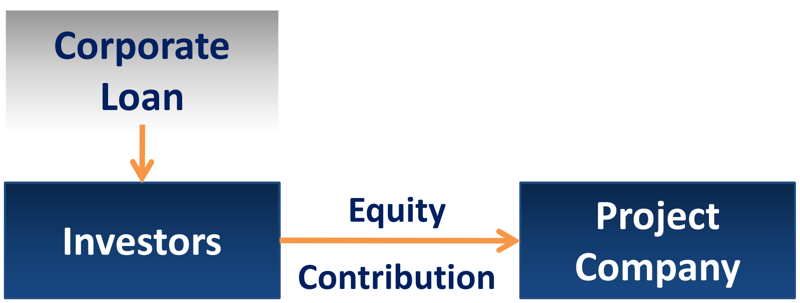
Developers/ Investors:

- Increasingly prefer to insulate themselves from the Project Company, therefore, limiting their risk exposure and preserving debt capacity.

PROJECT FINANCE

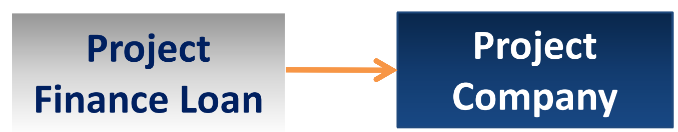
Corporate Finance

- Finances a Company (unlimited life)
- Based on Company's Overall Business
- On Balance Sheet Financing
- Focus on Corporate Credit
- Full Recourse to Investor/Sponsor



Project Finance

- Finances an asset (specified life)
- Based on project's cash flows
- Off-balance sheet financing
- Focus on risk allocation among parties
- Limited recourse to investor/sponsor
- High debt leverage



LENDERS' PERSPECTIVE

- One needs to think from the perspective of the lenders when structuring their project.
  - Lenders provide the bulk (typically > 70%) of the financing in project finance transactions.
  - Lenders want to minimize their exposure to risk; their upside is limited to the interest amount.
  - Lenders assess all the factors and risks that may impact the Project's ability to repay the debt and ensure that risks are adequately mitigated.
  - Lenders require the following:

1. Solid Project Economics
2. Satisfactory Risk Allocation and Mitigation
3. Credible and Creditworthy Counterparties

LENDERS' PERSPECTIVE: SOLID PROJECT ECONOMICS

- In project finance, projects are analyzed on a "stand-alone" basis.

- Project finance lenders focus their analysis on the project's cash flow, as they are lending against this single revenue stream from the project.

- Lenders to a project will make an assessment to determining that revenues are sufficient to:
  - pay the ongoing operating costs;
  - pay maintenance costs;
  - pay taxes; and
  - repay the loans (interest and principal).

All of the financial analysis of a project's economics is completed prior to funding and all the assumptions underlying the financial analysis need to be independently verified.

Lenders' Perspective: Satisfactory Risk Allocation

- Project finance lenders have limited recourse to the assets of an operating company or a sovereign government.
- Lenders want to ensure that if any problems occur they will still be repaid by the project.
- Lenders analyze closely the cash flow of the project they are funding to ensure that the cash flow of the project will not be disrupted for any reason.
- This process of project risk analysis and mitigation strategy is an important part of the lenders' assessment of the project.

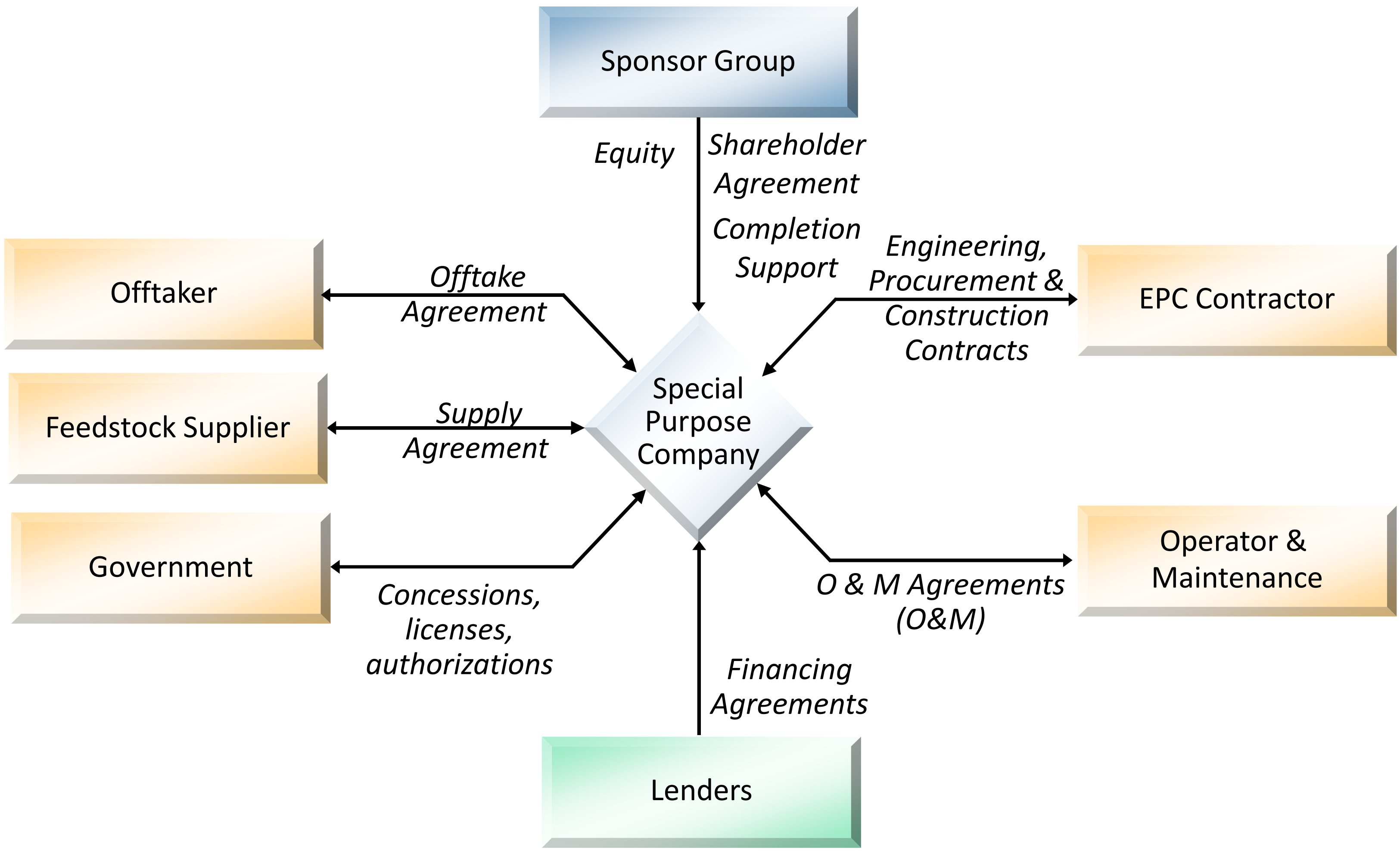
RISK ALLOCATION IN PROJECT FINANCE

- Philosophy of Risk Allocation: Each risk should be borne by the party most able to control or manage it.
  - Every individual risk is identified, considered, and mitigated.
  - Risk mitigation takes place by contractual allocation.
  - This philosophy is not unique to project finance, however, the process of contractually allocating risk and raising financing based on the total 'creditworthiness' of the risk allocation is.
- Mitigating risk requires considering all sources of support and choosing the mix to enhance the project with the lowest cost to the sponsors.
  - Objective is to create a bankable project that provides certainty to lenders and minimizes downside to equity providers.

Identify *– What could go wrong?*
Assess *– How bad could it be?*

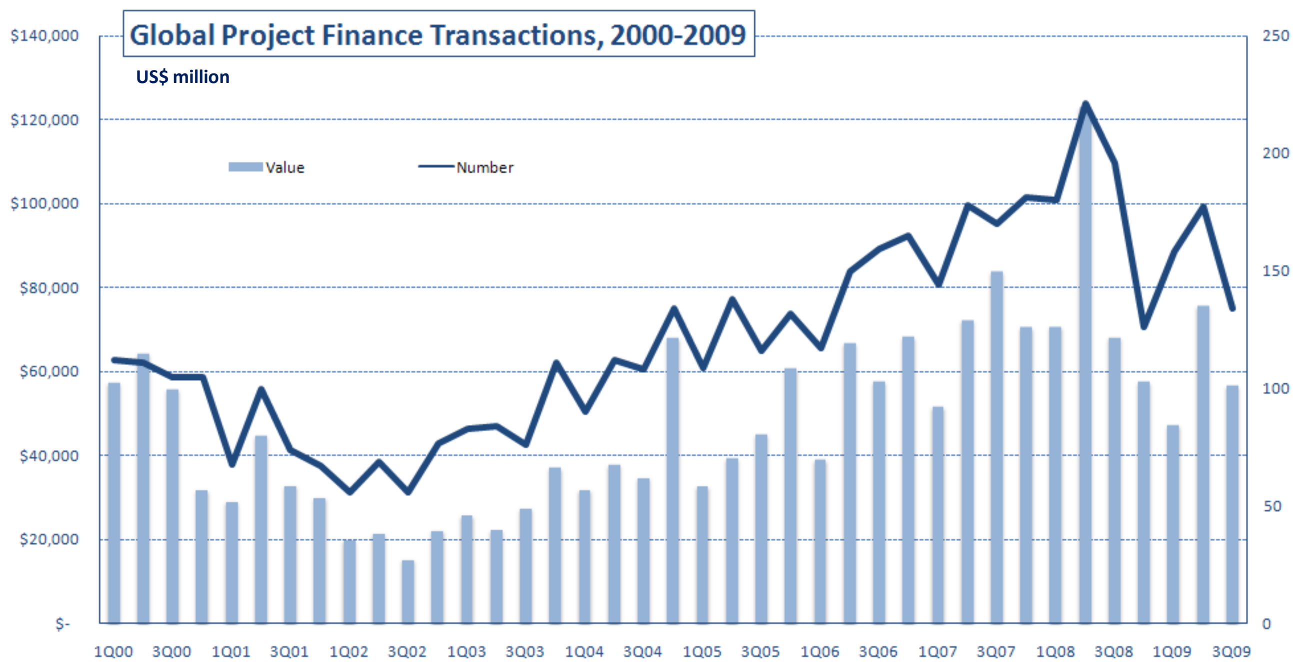
Mitigate *- Who can minimize the risk?*

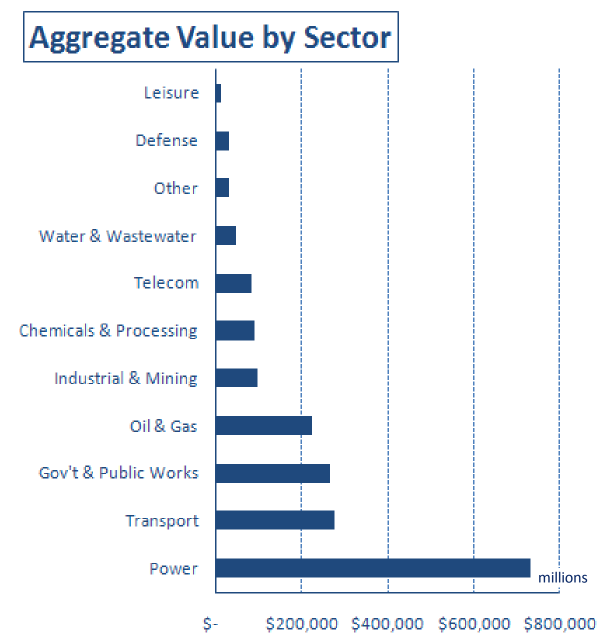
PPP and Project Finance – A Typical Structure



Global Project Finance Trends – All Sectors

- 2H 2008 saw a 35% value decline relative to 1H 2008.
- Many projects that reached financial close in late 2008 and 2009 were already in the pipeline prior to the start of the financial crisis.
- The World Bank estimates that projects totaling nearly $322 billion have been in some way affected by the credit crisis; nearly half have felt a major impact.

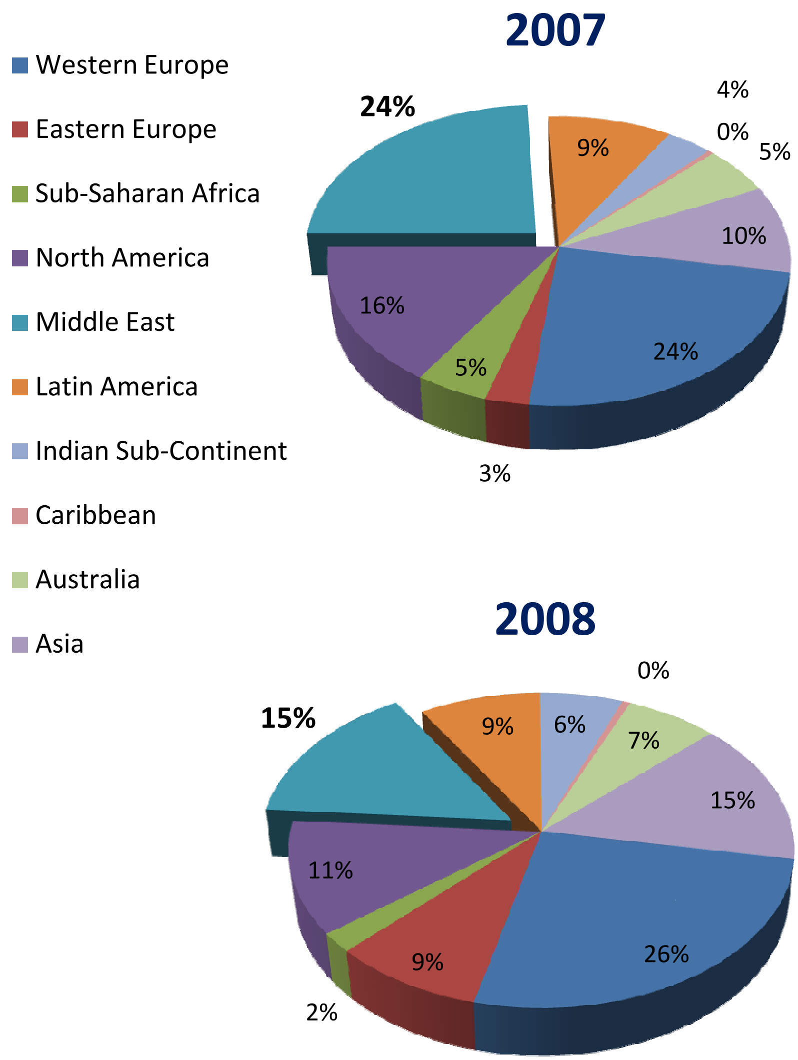




Source: Dealogic

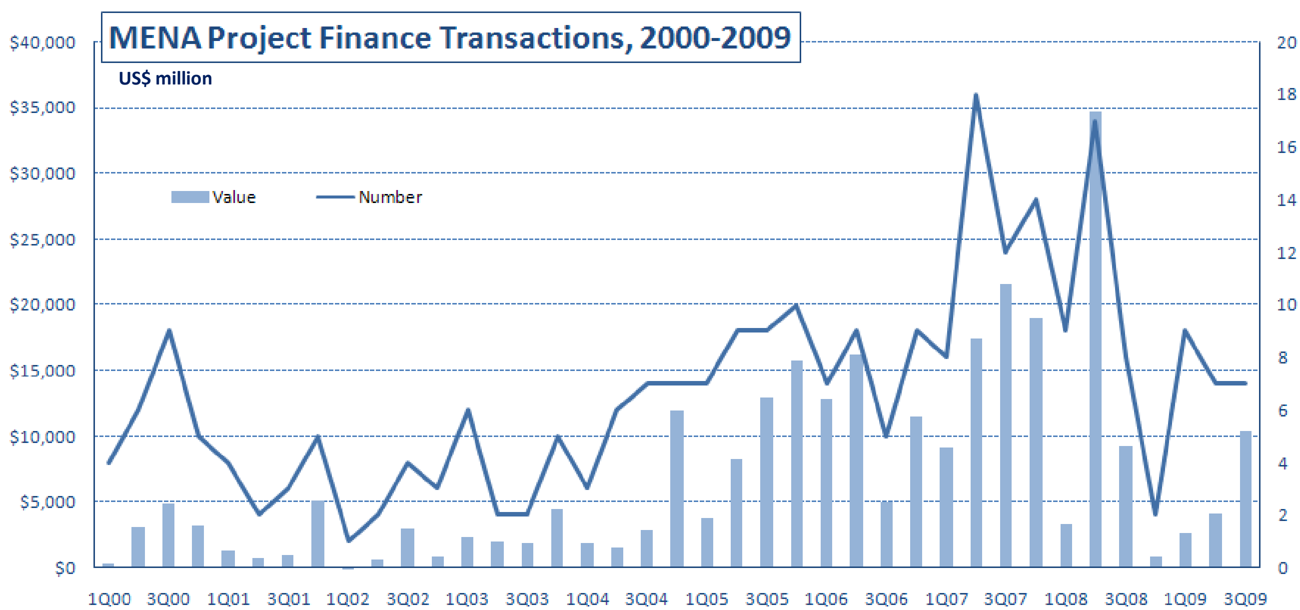
Project Finance Trends - MENA

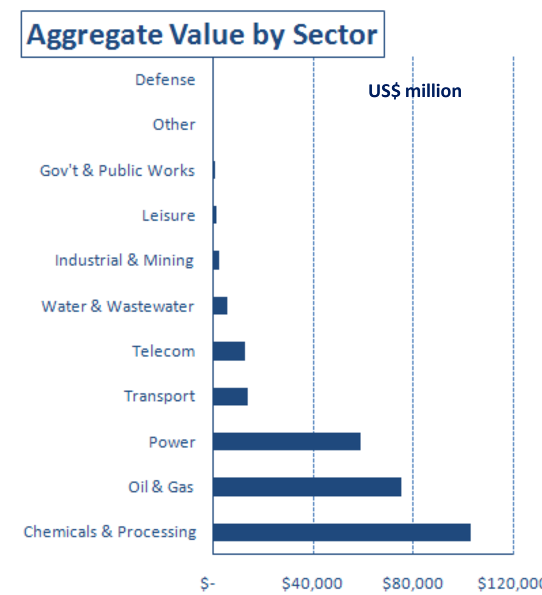
- MENA represents a major region for project finance activity.
  - 2nd in aggregate value for total projects closed in 2007 and 2008.
- Petrochemicals, oil & gas, power generation and transportation projects receiving the majority of funding.
- As of October 2009, 25 projects have closed in 2009 totaling US $21 billion in aggregate value.
  - Dolphin: ~US$ 4 billion
  - Shuweihat II: ~US$2.6 billion



PROJECT FINANCE IN MENA – ALL SECTORS

- 4Q 2008 was the worst quarter for project finance in MENA since 2002 – a <u>97% decline</u> relative to 2Q 2008 levels. Only two projects reached financial close.
- Markets are recovering somewhat, but large transactions have faced difficulties. Many projects delayed.
  – Ex. Citadel Musturud Refinery (delayed), Al-Zour Refinery (delayed and EPC contract cancelled)

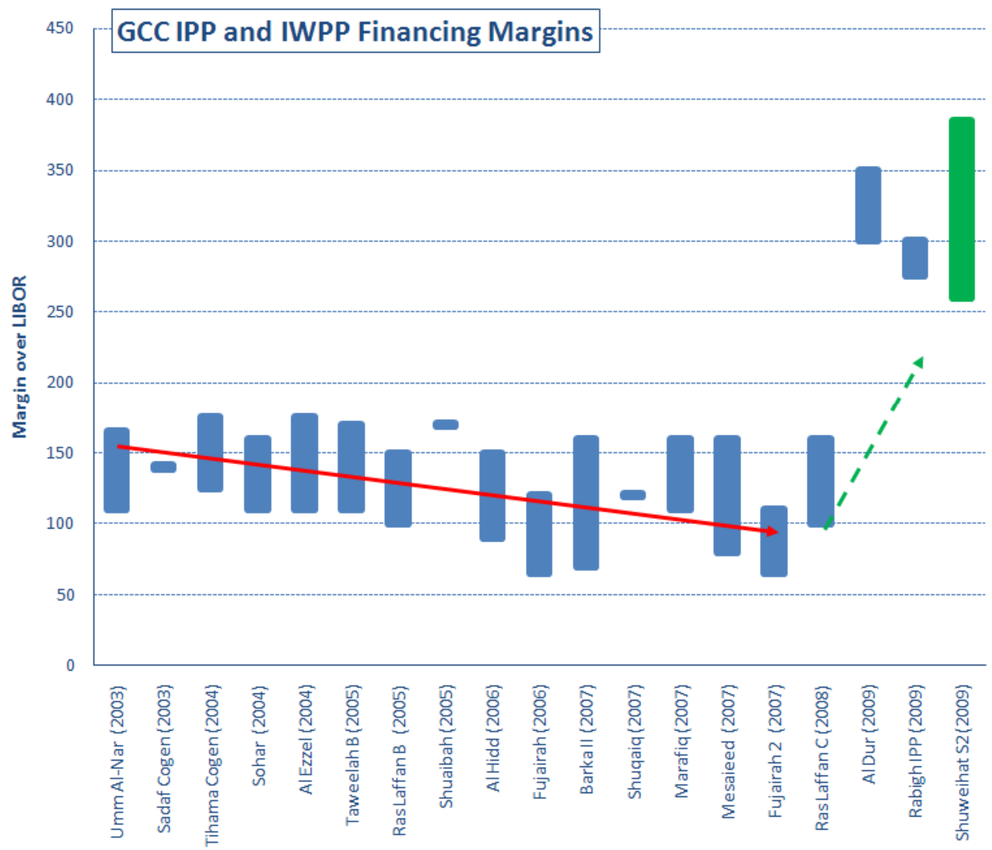




Source: Dealogic

THE COST OF FINANCE: GCC POWER SECTOR

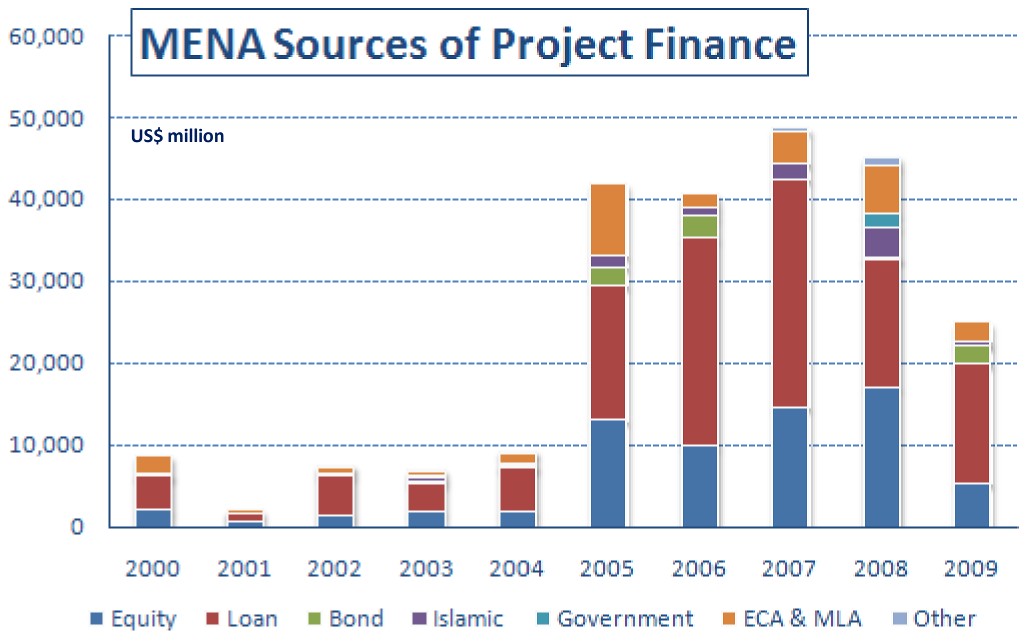
- While projects have been able to reach close, margins have risen over 100bp.
- Project structures and sources of finance are adapting to the challenging market:
  - **Growing use of mini-perm structures**: Al Dur initially sought 20-year debt but closed on an 8-year mini-perm.
  - **Increased reliance on ECA financing**: Shuweihat S2, Al Dur, and Rabigh have all brought ECAs into the financing process.
  - **Rising public involvement**: Ras Al-Zour was converted from a concession to a government-owned EPC deal.

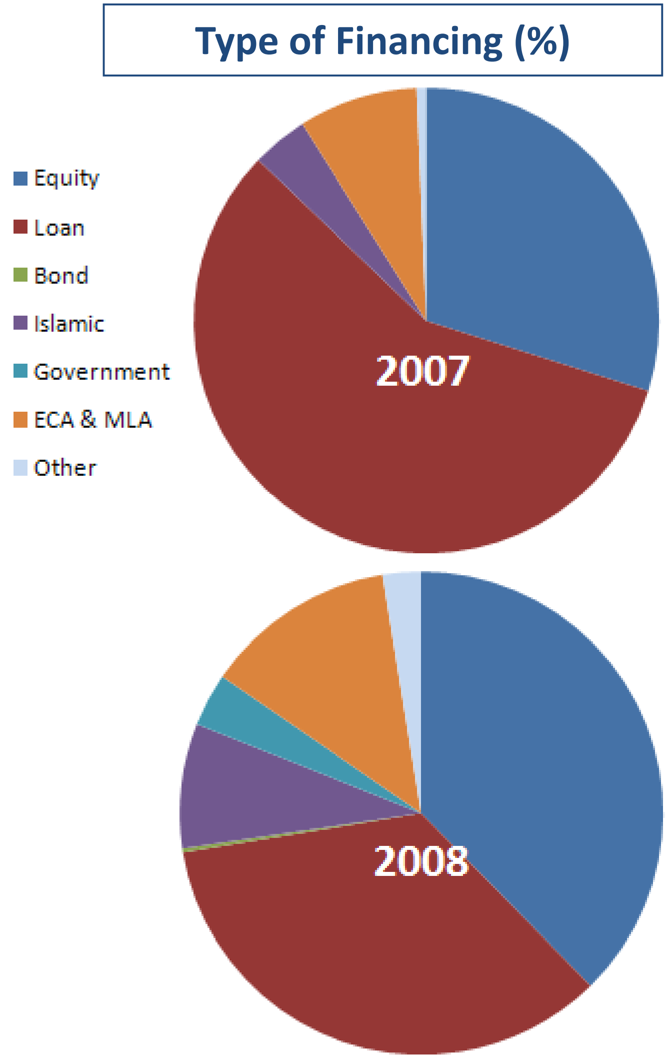


Sources: Dealogic, Project Finance International, Infrastructure Journal

Finding New Sources of Liquidity

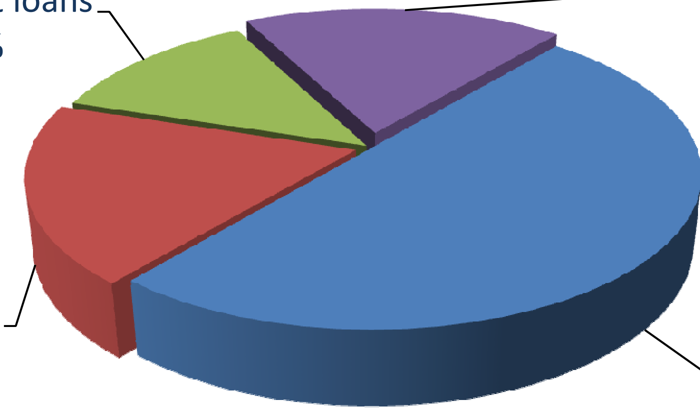
- While ECAs, MLAs, and Islamic finance may have higher costs and longer arranging times than commercial bank debt, these options have become increasingly popular as a source of new liquidity.





Sources: Dealogic, figures exclude acquisitions and refinancings

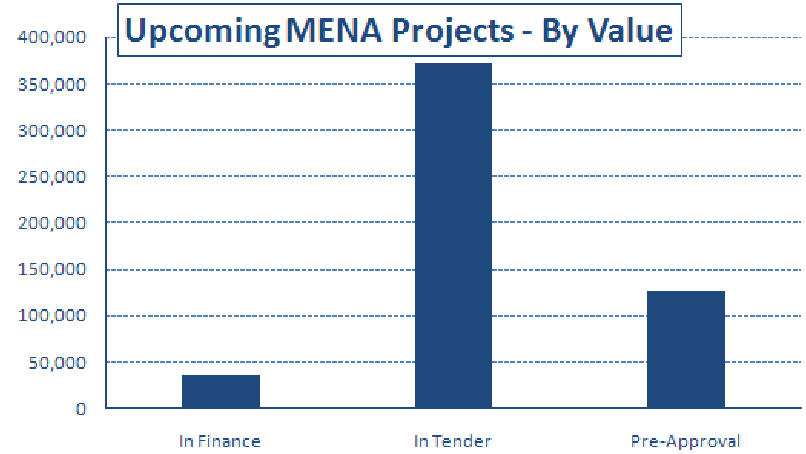
Case Study: Al Dur IWPP

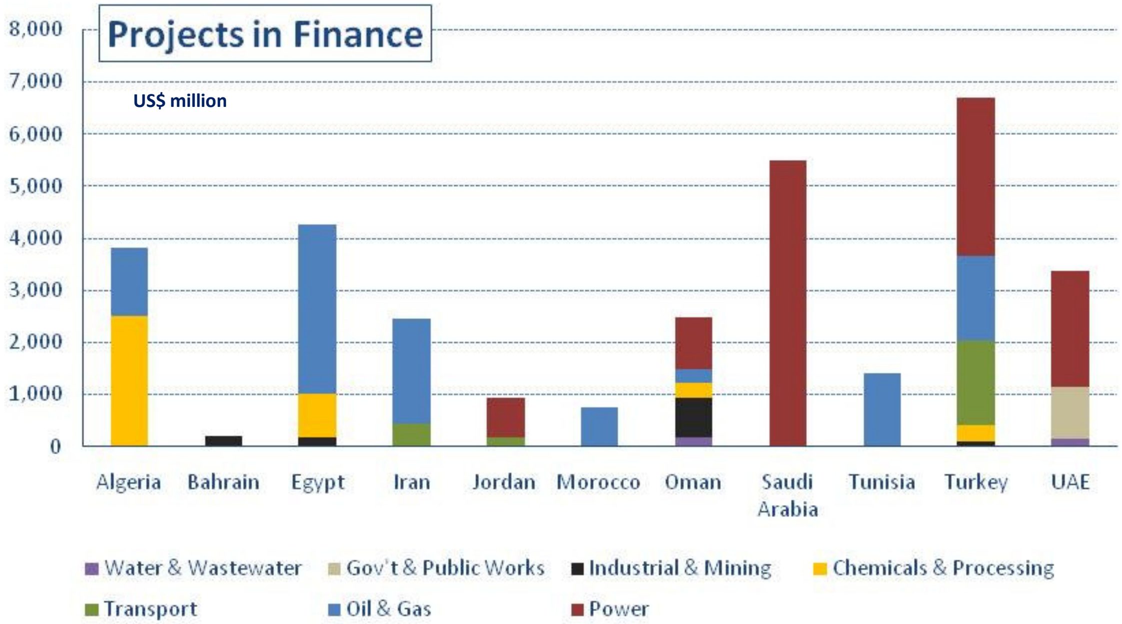


- Cost: US$2.1 billion
  - US$1.6 billion mini-perm debt financing structure (first for a Middle East power project)
- Used commercial banks, export ECAs, and Islamic financing.
- Debt maturity: 8 years
  - 100 per cent cash sweep after 5 years.
- Financial close: 29 June 2009
- Sponsors: GDF Suez (45%), Gulf Investment Corp. (25%), Capital Management House (15%), Social Insurance Organization of Bahrain (10%) and Instrata (5%).
- Offtake: 25-yr PWPA with Bahrain's Electricity and Water Authority
- Start of operations: Summer 2010

THE FUTURE FOR PROJECT FINANCE IN MENA

- MENA still has a large project pipeline, with 34 projects totaling $35.5 billion in value seeking project financing.





- The energy sector accounts for the majority of projects (by value) seeking project financing in MENA:
  - 36% in power
  - 30% in oil & gas
- The GCC accounts for 33% of the value of projects in finance.

Source: Dealogic

Project Finance: An Overview of Public-Private Roads

COMMERCIAL STRUCTURE: TOLL ROAD (OPTION 1)

Government Role:

- Contracting Authority
- Source of project revenues (shadow tolls)

Private Sector Role:

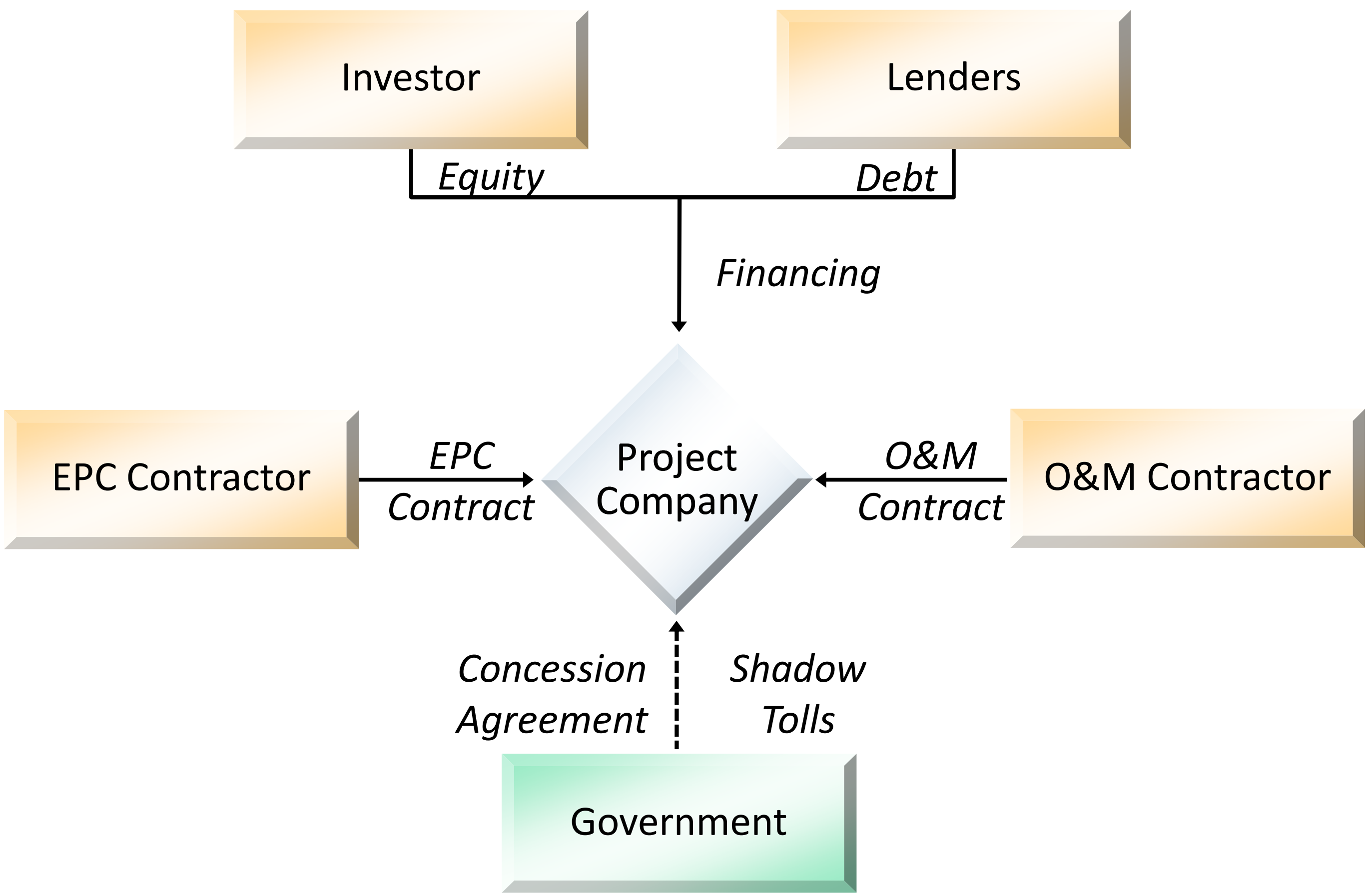
- Operation, construction, and maintenance

Toll Payments:

- No tolling of users
- Government makes shadow toll payments

Road Ownership:

- Concessionaire



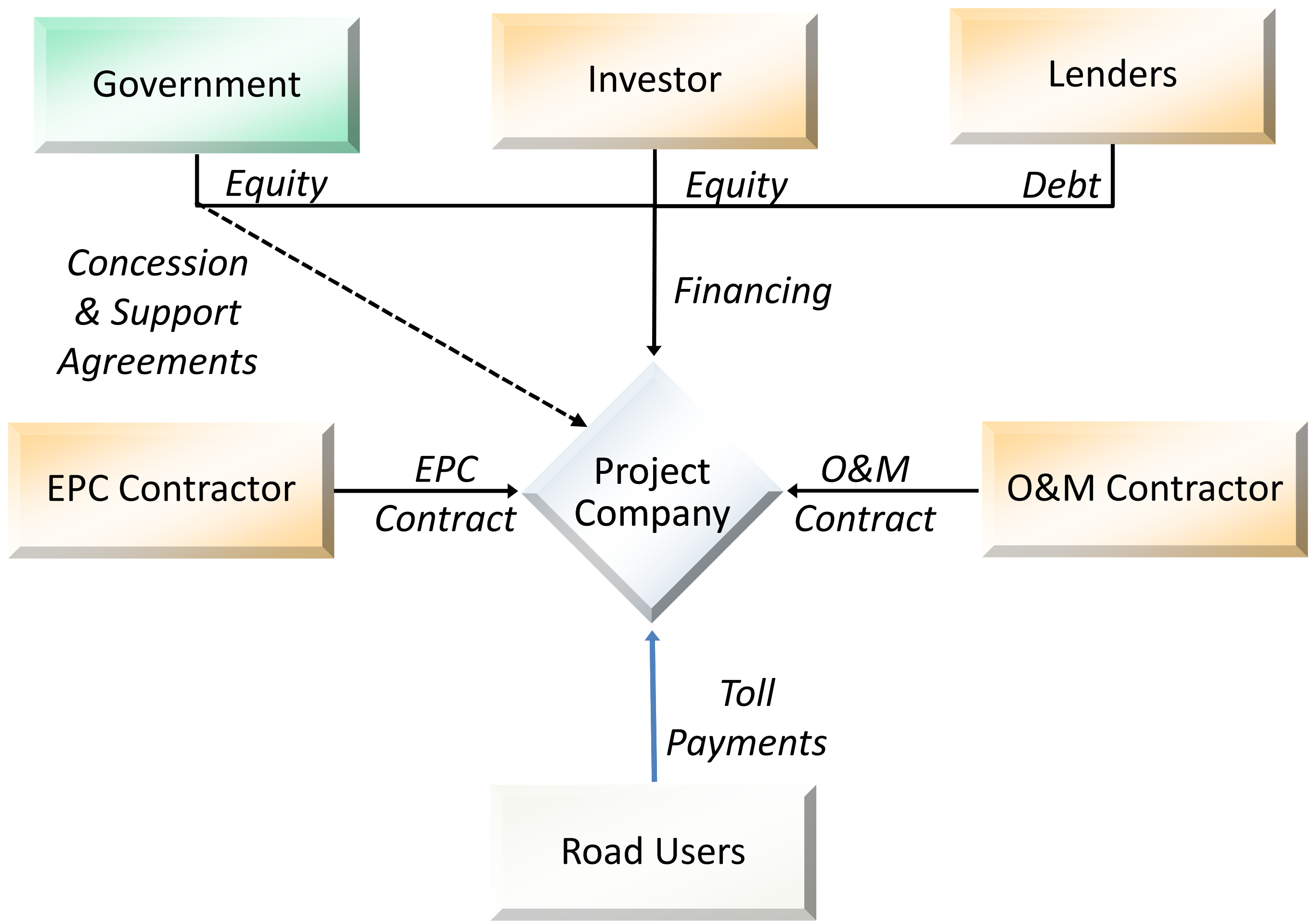
Commercial Structure: Toll Road (Option 2)

Government Role:
- Contracting Authority
- Co-investor
- May provide project support in the form of revenue shortfall provisions

Private Sector Role:
- Co-investor and operator of road concession

Toll Payments:
- From end-users directly to Project

Road Ownership:
- Joint government and private ownership for duration of concession



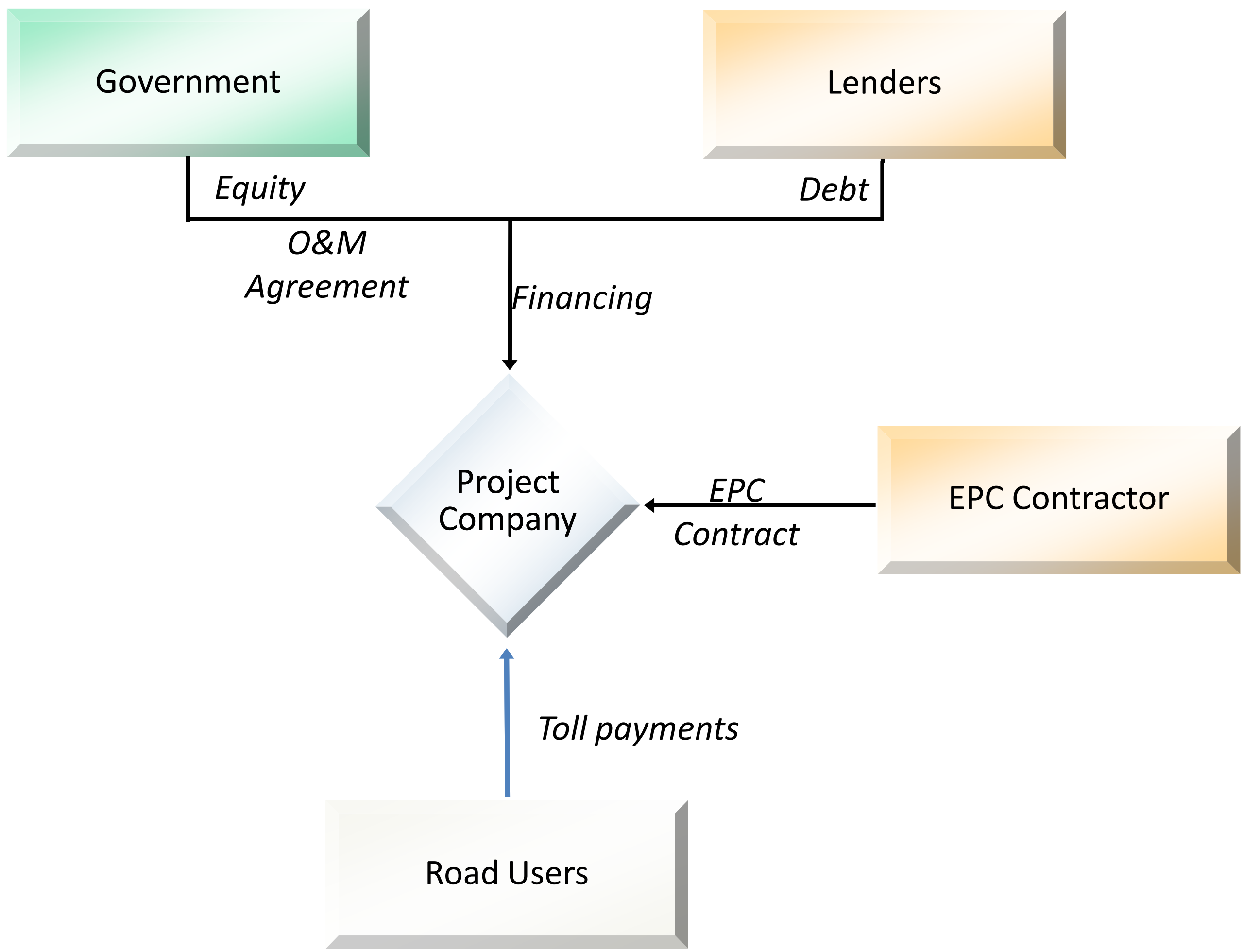
Commercial Structure: Toll Road (Option 3)

Government Role:
- Owner and operator of road

Private Sector Role:
- Construction only

Toll Payments:
- From end-users directly to Project

Road Ownership:
- Government



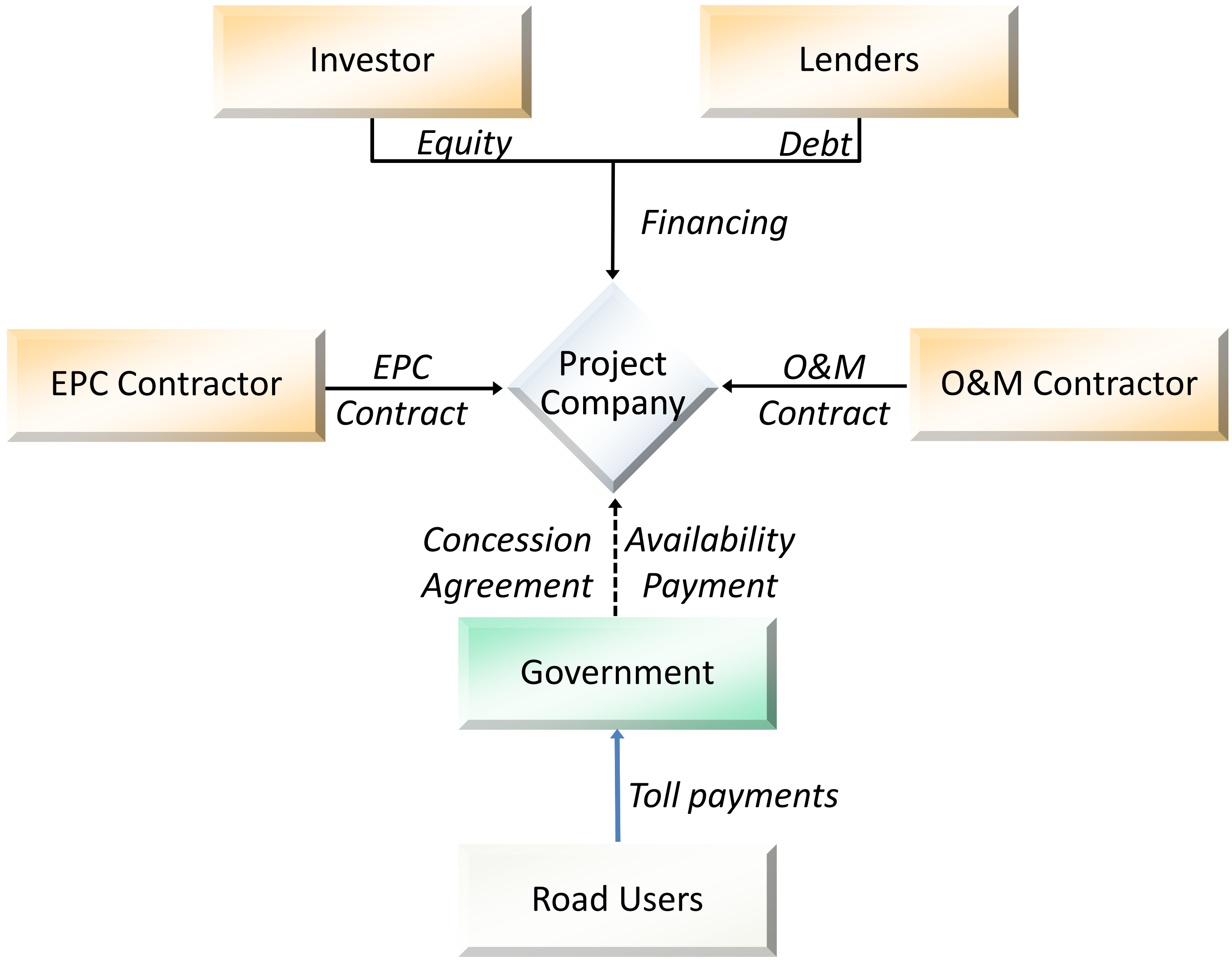
COMMERCIAL STRUCTURE: TOLL ROAD (OPTION 4)

Government Role:
- Contracting Authority
- Source of Project revenues

Private Sector Role:
- Owner and operator of road concession

Toll Payments:
- From end-users to Government

Road Ownership:
- Private concessionaire for duration of concession period



CASE STUDY: I-595 CORRIDOR

The I-595 Corridor, located in Broward County, Florida was the first PPP deal in Florida. The deal was innovative in its use of availability payments to mitigate traffic risk for the private concessionaire. The project reached financial close in 1Q 2009, in the midst of the credit crisis.

- Project Overview:
  - 35-year concession to build, operate and maintain three new toll lanes. The project involved reconstruction, widening, and resurfacing of a 10.5 mile stretch of highway.
  - Revenues to the project company came in the form of availability payments from the Florida Department of Transportation rather than direct tolls, effectively eliminating traffic risk.
- Taylor-DeJongh was advisor to TIFIA, a U.S. federal credit program for innovative transportation projects and a lender to I-595.
  - Evaluated the borrower’s financing plan.
  - Structured the TIFIA loan.
  - Advised in the negotiating term sheet.
  - Assisted in negotiating the TIFIA loan agreement and other closing documents.

CONCESSION AGREEMENT HIGHLIGHTS

- Term is 35 years.

- Concessionaire is given the exclusive right to operate the Project while FDOT retains ownership and right to develop any additional infrastructure.

- Concessionaire is responsible for:
  - Securing 100% of the Project's financings;
  - All construction costs;
  - Operations, maintenance and renewal work on the Project, with annual budget approved by FDOT.

- FDOT sets and collects tolls and compensates Concessionaire with:
  - Availability Payments ("AP") over the operating life of the Project, paid quarterly in arrears.

Project Structure – I-595

Government Role (FDOT):

- Concession awarder
- Source of revenues (availability payments)

Government Role (Federal):

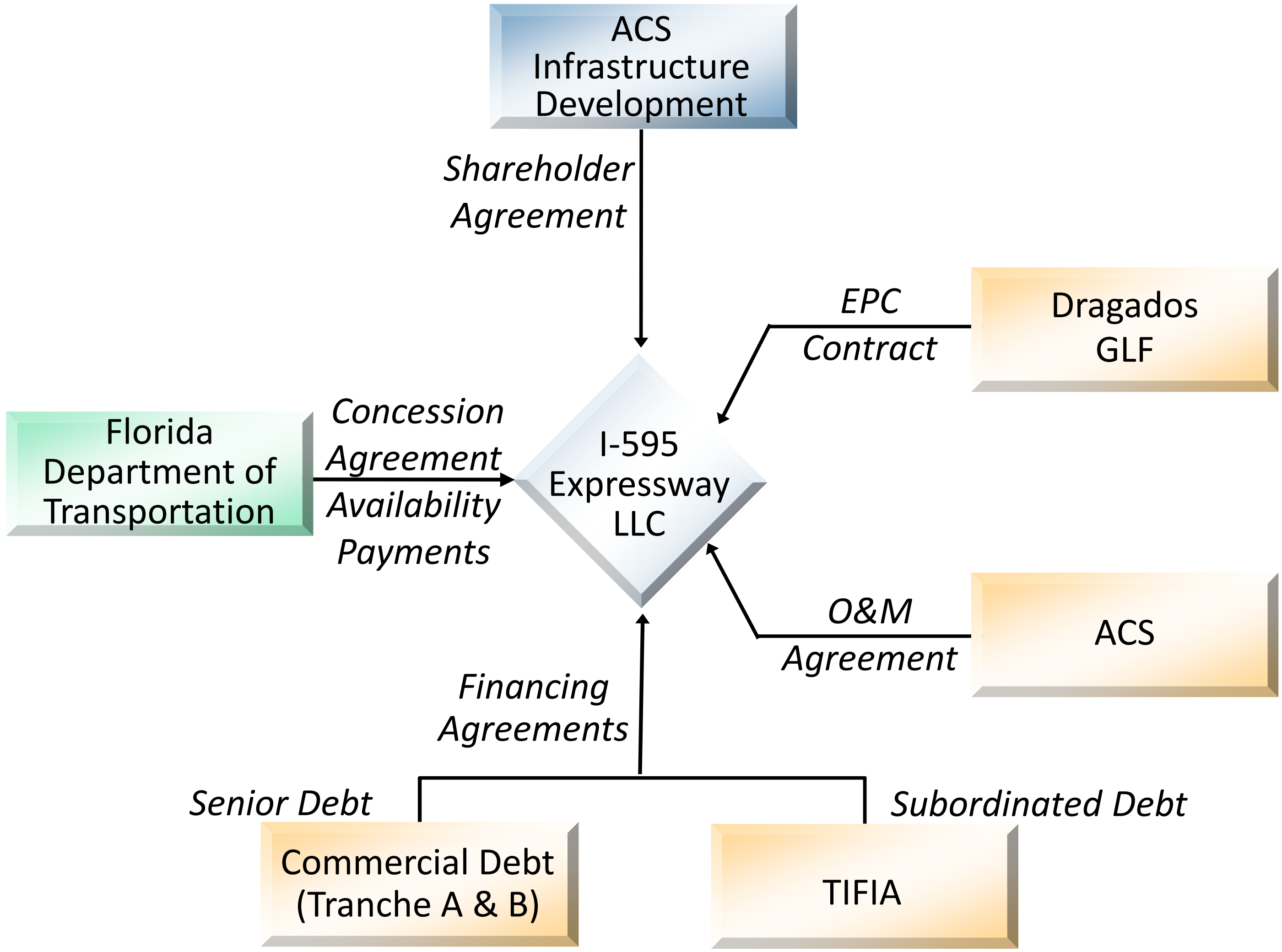
- Subordinated lender

Private Sector Role:

- Concessionaire
- Operator
- EPC contractor

Toll Payments:

- From end-users directly to FDOT



IMPLICATIONS FOR SYRIAN PPPS

- To ensure the success of PPP, Syria must address key requirements:
  - Promote a stable macroeconomic environment,
  - Demonstrate sufficient government support, including firm public commitment.
  - Ensure a suitable legal and regulatory framework for infrastructure projects.
- The financing environment for both projects and companies has become more challenging – for a PPP to be successfully project financed, projects must now be even more carefully structured, with strong counterparties.
- Syria is in a market competing for the attention of bidders and lenders – against a large backlog of projects in the GCC.
- The use of ECAs, MLAs, Islamic Finance and government funds have become more prevalent as debt markets have tightened.
- Consider procurement plan for the project – and how that ties with ECAs.
- Start with simple, small and conventional projects and financing plans – have one success to establish credibility with bidders and lender, before launching multiple projects or a billion dollar project in the market.

Washington DC

1101 17th St, NW
Suite 1220
Washington, DC
20036
United States of America

T +1 202 775 0899
F +1 202 775 1668

contacttdj@taylor-dejongh.com

London

34 Smith Square
London
SW1P 3HL

United Kingdom

T +44 20 7233 4000
F +44 20 7808 1801

tdjlondon@taylor-dejongh.com

Bahrain

Office 2207/2209
Almoayyed Tower
Seef District
PO Box 11487
Manama
Bahrain

T +973 17567925
F +973 17567921

tdjme@taylor-dejongh.com