Project Financing

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Asset-Backed Securities

Project Financing

Stand-alone, non-recourse, multi-stake, "production payment financing"

Structure?
Participants?
Funding sources?
Risks?

Project Financing (Summary)

Stand-alone, non-recourse "production payment financing"
Sponsor's vehicle company structures multi-stake finance
Sources: govt development financing, IBRD/IFC, sponsor loans, supplier credits, customer credits, institutional investors, banks, lease financing, equity
Risks: resource quantity, input costs, technical, timing, pre-completion, demand, operating, force majeure, political
Risk sharing and mitigation

Financing Sources

Sponsor
- Loans
- Equity

Stakeholder credits
- Suppliers
- Purchasers

Gov't Development Banks, IBRD/IFC, Eximbanks
**Financing Sources**

- Banks, Institutional Investors, Leasing Companies
- Sponsor
  - Loans
  - Equity
- Stakeholder credits
  - Suppliers
  - Purchasers
- Gov't Development Financing, IBRD/IFC, Eximbanks

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**Project Financing**

**Definition**
- **Lending** to a single purpose entity for the acquisition and/or construction of a revenue generating asset with limited or no recourse to the sponsor
- **Repayment** of the loan is solely from the revenues generated from operation of the asset owned by the entity
- **Security** for the loan
  - all shares and interests in the entity
  - real property
  - all contacts, permits
  - authorizations, etc.; and,
  - all other instruments necessary for continuing project operations

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**Steps**
- Project Identification & Resource Allocation
- Risk Allocation & Project Structuring
- Bidding & Mandating Contracts
- Due Diligence & Documentation
- Execution & Monitoring
- Construction Monitoring
- Term Loan Conversion & Ongoing Monitoring

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**Benefits of Project Financing**

- Limitation of Equity Investment to Project's Economic Requirement - Enhanced Returns
- Risk Sharing and Diversification
- Accounting Treatment Preserves Corporate Borrowing Capacity
- Access to Long Term Financing
- Tax Benefits
- Political Risk Mitigation

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**The Risks**

- Political
- Resource & input
- Technical
- Construction
- Legal
- Economic

**Eurotunnel: The Risks and the Remedies**

<table>
<thead>
<tr>
<th>Category</th>
<th>Nature</th>
<th>Remedy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Political</td>
<td>Nationalization</td>
<td>Legal</td>
</tr>
<tr>
<td></td>
<td>Gov't interference</td>
<td>Treaty ratified</td>
</tr>
<tr>
<td>Technical</td>
<td>Process</td>
<td>Use existing technology</td>
</tr>
<tr>
<td></td>
<td>Effect on completion</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Repairability</td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td>Delays</td>
<td>Use top experts</td>
</tr>
<tr>
<td></td>
<td>Overruns</td>
<td>Performance bonds</td>
</tr>
<tr>
<td></td>
<td>Repairability</td>
<td></td>
</tr>
<tr>
<td>Legal</td>
<td>Access to control in default</td>
<td>Security interests</td>
</tr>
<tr>
<td></td>
<td>Fire, injury, etc liability</td>
<td>Default defn</td>
</tr>
<tr>
<td>Economic</td>
<td>Price competition</td>
<td>Market studies</td>
</tr>
<tr>
<td></td>
<td>Rail links</td>
<td></td>
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</tbody>
</table>
**Sample Structure**

- **Sponsors / Shareholders**
- **Equipment Supplier**
- **Contractor**
- **Feed Stock (e.g., fuel) Supplier**
- **Operator**
- **Warranties and Supply Agents**
- **Offtake (e.g., power purchase) Agreement**
- **Arranging Bank**
- **SINGLE PURPOSE PROJECT COMPANY**
- **Syndicate Banks**
- **Other Project Participants:**
  - Currency and Interest Rate Hedge Providers
  - Multilaterals and EDA’s
  - Legal Counsel
  - Technical Consultants

**Limpopo Hydro**
- **US$302 million project for Zimbabwe and regional electricity supply**
- **Financing from**
  - UK banks
  - US banks/PEFCO with Export g’tee
  - US insurance co’s
- **8.5-year lease financing**

**Financing of Limpopo Hydro**

<table>
<thead>
<tr>
<th>Financing Source</th>
<th>Amount, US$ equiv.</th>
<th>Currency</th>
<th>Guarantees</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>UK banks</td>
<td>$15 million £</td>
<td>XYZ</td>
<td>LIBOR + 2.65%</td>
<td></td>
</tr>
<tr>
<td>US bank syndicate, then PEFCO</td>
<td>$244 million US</td>
<td>US Eximbank and XYZ</td>
<td>LIBOR + 30%, then T+0.75</td>
<td></td>
</tr>
<tr>
<td>Private placements with US insurance companies</td>
<td>$34 million US</td>
<td>XYZ</td>
<td>SLIBOR + 2%, then T+4.00%</td>
<td></td>
</tr>
</tbody>
</table>

**Bakun?**
- **Cost:** RM15 billion ($6 billion)
- **Completion:** 2002?
- **Capacity:** 2,400 megawatts
- **Contract for sale to Tenaga:**
  - Years 1-5: 16.5 sen/kwh
  - Years 6-30: 17 sen/kwh

**Asset-Backed and Project Financing**
- **Collateralized debt**
- **Securitized loans**
- **Non-recourse project debt -- future payments rather than assets are the collateral in the SPV**
- **Basic question:** When is an asset worth more to investors outside the company than inside it?
Case Studies

- Ras Laffan Qatar/Korea
- YPF Argentina/Oil Trading Corp
- West Java Power Project

Questions:
- Who is the issuer?
- What assets does it have?
- What are the risks, and how are they handled?

Ras Laffan

- Who is the issuer?
  - Ras Laffan LNG Co. Ltd. (Qatar)
  - But Security Trustee (IBJ) plays unusually major role

- What assets does it have?
  - Natural gas reserves;
  - LNG take-or-pay Sale and Purchase Agreement with Korea Gas;
  - Security Trust Agreement; Project Coordination Agreement; loan refund agreement, etc.

Ras Laffan: Natural Gas Project Finance

YPF Argentina/Oil Trading Corp

- Who is the issuer?
  - Oil Trading Corp, Cayman Is. SPV

- What assets does it have?
  - No oil, just purchase and sale agreements

- What are the risks, and how are they handled?
  - Seller: Political, production
  - Buyer: Credit, legal
  - Economic
**West Java Power Project**

- **Who is the issuer?**
  - Pratama SPV

- **What assets does it have?**
  - Loan to Dayalistrik Pratama

- **What are the risks, and how are they handled?**
  - Political; Engineering; Coal supply; Default on Purchase Agreement; Economic

**West Java Project Financing**

- **Project stage:**
  - Uncompleted coal-fired power plant, generating power
  - Has multi-year power purchase agreement with utility
  - Currently has bank financing
  - Sponsors seeking to extend financing and reduce cost by tapping the debt securities market

**Proposal:**

- Sponsor issues “infrastructure revenue bonds” to refinance bank loans
- Bonds to be issued with 19 year maturities - longer than the term on the bank loans
- May have fixed rate; distributed in US, Euro or domestic bond market
- Int. and principal secured by contract revenues
- May have 100% guarantee from monoline insurance company

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