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PPP FINANCING DURING THE CRISIS

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There have been some very mixed signals about how the global financial crisis has affected PPPs during the past year. According to Reuters data, debt issuance for project finance rose 6.3 percent in 2008 to \$262.3 billion globally¹. However, some major players have been devastated by the crisis. Royal Bank of Scotland (RBS) exited the project finance market in February 2009 as part of a major restructuring. The bank experienced an annual loss of £24.1 billion in 2008, the largest ever in UK corporate history². This was the same year the bank was ranked the lead Mandated Arranger for project finance lending globally. Macquarie Group Ltd.'s share price and earnings are half what they were a year ago. Babcock and Brown Ltd. was placed into voluntary administration on March 13.

While global debt markets have choked, there still remains a large amount of private equity seeking infrastructure investments. Globally, infrastructure funds raised \$24.7 billion in 2008, compared to \$34.3 billion in 2007 and \$17.9 billion in 2006. There are currently more than 75 infrastructure funds seeking to raise \$100 billion. Much of the funds already raised have had trouble finding projects. The problem for them is not lack of financing but lack of suitable projects. For example, Goldman Sachs raised \$6-8 billion for an infrastructure fund in 2006 and has yet to find projects to invest the full amount. Pension funds around the world are seeing positive returns from their infrastructure investments as their investments in other asset classes take a dive.

In this environment, what projects are reaching financial close? Do they hold any lessons for other projects or for the overall PPP market? Below, I review three projects that have recently closed and try to glean some indicative information from them that can help to understand the current market and predict future developments.

Florida I-595

The Florida I-595 PPP is a 35-year concession on a 10.5 mile portion of the highway in Broward County, north of Miami. The deal reached financial close on March 3, 2009. It is a \$1.8 billion project including: \$800 million in bank debt; \$600 million in TIFIA (Transportation Infrastructure Finance and Innovation Act) lending; \$232 million from the Florida Department of Transportation; \$200 million in equity; and \$10 million from revenue. The bank consortium includes BBVA, Caja Madrid, Calyon, Fortis, SG and Santander. ACS Dragados is the consortium leader and only equity investor.

This is the first PPP in the US to use an availability payment scheme. Even though the road will be tolled, the bidders were not comfortable assuming market risk given the current economic climate. The consortium will receive payments of \$63.98 million for 30 years. This is a major development for the US market in which toll roads

¹ Infrastructure Investor February 27, 2009. "RBS to Exit Project Finance amid £24.1bn Annual Loss".

² Infrastructure Investor February 27, 2009. "RBS to Exit Project Finance amid £24.1bn Annual Loss".

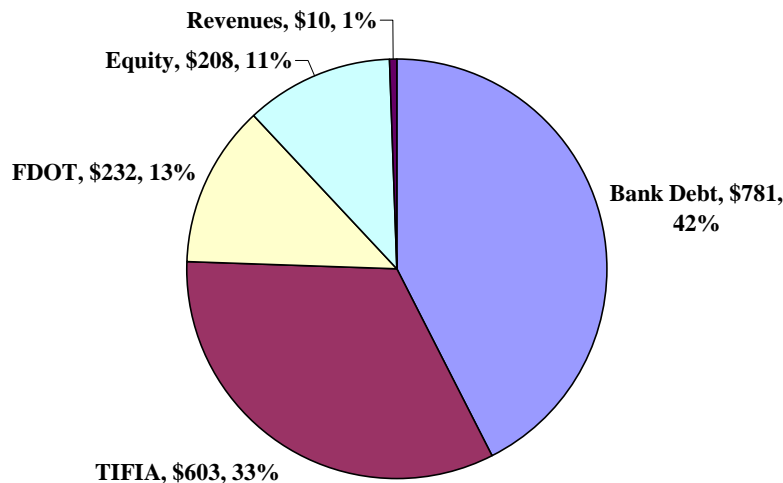
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are common and usually provide the revenue for concessionaires on highway projects. Given the lower volumes of traffic as a result of the financial crisis, it is likely that availability payment schemes will become more popular not just in the US but globally.

In addition to the federal TIFIA loan, the Florida State Department of Transportation contributed 13 percent of the financing for the project. That brings total public sector financing to 46 percent of the project costs. This is an indication of a true partnership where the public and private sectors are in fact cofinancing the project. Private financing is used to leverage public financing, not to replace it. Private financial sources have become scarcer. The private financing that is available is risk averse and more comfortable investing in projects that have a high level of public sector financing – in addition to risk sharing such as under availability payment schemes. It is likely that more projects will see a higher level of public sector financing. The two other projects analyzed below are examples of this new trend.

Construction on the Florida project is expected to begin in June and be completed within five years³. See the graph below for a breakdown of the project's financing. Project website: <http://www.i-595.com/default.aspx>.

I-595 Financing (US\$m) Total = US\$1.8b



While the closing of the I-595 deal was a welcome positive sign for the PPP market especially in the middle of a financial and economic crisis, the Port of Miami

³ Project Finance March 2009. "Iridium Closes I-595 in Florida" and PFI February 25, 2009. "Club for I-595".

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tunnel project failed to reach financial close at the same time because of the lack of private financing.

Poland A1 Phase II

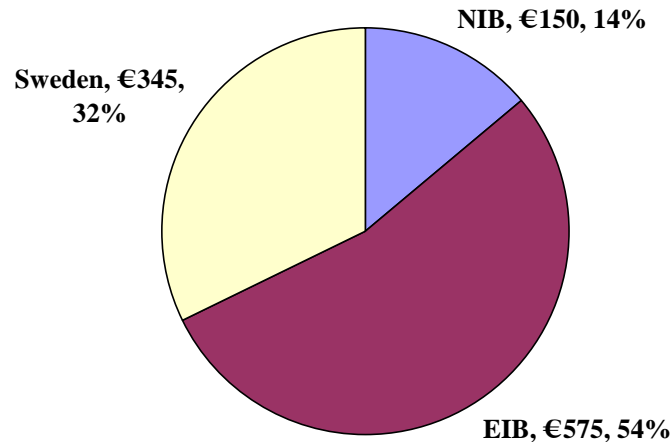
The A1 motorway in Poland is a planned motorway which will run from the port city of Gdansk on the Baltic Sea to the Polish-Czech border. The highway will be a part of the European route E75. The total length of the motorway is planned to be 568 km.

Phase I of the Poland A1 was launched in July 2005 and the road was opened to traffic in October 2008. It consists of a 90km section of road from Gdansk to Nowe Marzy. Gdansk Transport Company (GTC), the concessionaire for Phase I was also selected for Phase II of the Project. The members of GTC are: Skanska Infrastructure Development AB, one of the world's largest construction services companies; John Laing Infrastructure Ltd, a leading international investor and developer of PPPs; NDI Autostrada Sp. Z o.o, a subsidiary of NDI, a private Polish construction company; and Intertoll Infrastructure Developments BV, a subsidiary of Group Five, one of South Africa's largest construction groups.

In December 2008, financial close was reached on Phase II of the project, which will extend the southern section of the road 60 km to the City of Torun. Financing for Phase II came from European Investment Bank (€75), Nordic Investment Bank (€150) and Swedish Export Credit Corporation (€45) for a total of €1.07 billion of financing. The financing arrangements for Phase II are significant in that they do not include any private sources. The project was structured as PPP but in the end no private finance could be found for the project. So, the bilateral and multilateral agencies were tapped to fill the gap. Project website: <http://www.a1-autostrada.pl/en/>

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Poland A1 Phase II (€m) Total = €1.07b



While the fact that the A1 Phase 2 was able to reach financial close can be considered a good sign for the PPP market in Poland and beyond, the A2 highway, which runs East-West in Poland, failed to reach financial closure in March 2009. Since then, the AWSA consortium consisting of Strabag, Meridiam Infrastructure and Polish Electroenergy Group have obtained a guarantee from the Polish government for the project's debt. The project's financial advisors, Deutsche Bank and Calyon have now given lenders until the middle of June to come up with €600 million of financing. This is in addition to a €1 billion loan expected from the EIB. In this case, we see both the increase of public financing as well as an increased demand for public sector guarantees.

Kenya Lake Turkana Wind Power (LTWP) Project

The Lake Turkana Wind Power (LTWP) project aims to add 300 MW of electricity to Kenya's national grid by June 2011, increasing electricity supply by approximately 30 percent. The LTWP consortium, including Anset Africa, a project development and management company, and KP&P, a Dutch wind developer, will build a wind farm of 353 turbines each with a capacity of 850 KW. The project will address the urgent need for additional electricity supply for Kenya which is expected to face an electricity deficit in 2012 if no new capacity is added.

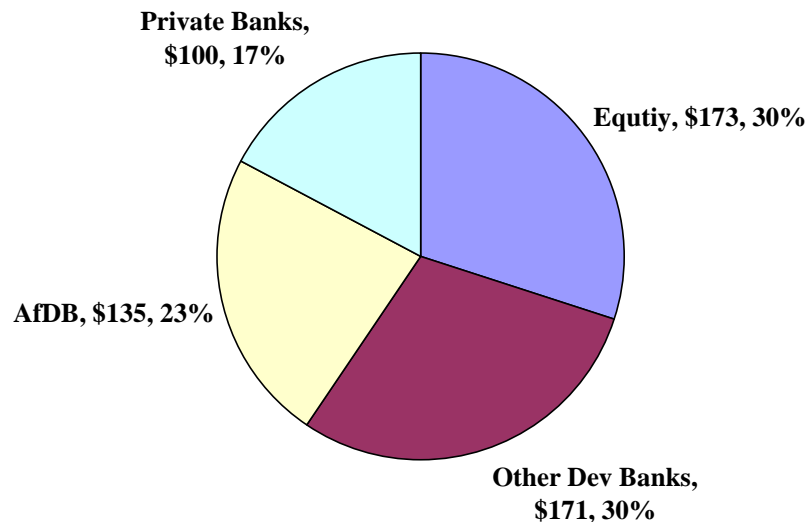
The African Development Bank (AfDB) originally committed to provide 30 percent of the financing for the project. In May, however, the bank agreed to act as Mandated Lead Arranger for the \$405 million of financing covering 70 percent of the project cost. AfDB will lend the project \$135 million directly and seek additional

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financing from other development institutions as well as private sector sources. The LTWP consortium will contribute 30 percent equity to the project.

Again, this shows the increased role of the public sector in PPP projects. In this case, the AfDB has stepped up its role from one of the lenders to the Mandated Lead Arranger. And, while it plans to source some of the financing for this project from the private sector, it may in the end face the reality that only public financing will be available for the project. This project also features a high level of equity at 30 percent. While a few years ago, 90/10 was the standard debt/equity ratio for projects, we now see increasing demands for equity in some projects. This is a more traditional approach to project finance that saw 70/30 or even 60/40 as the normal ratio in the 1980s.

Kenya LTWP Likely Financing (US\$m) Total = \$579m



Conclusion

By reviewing these three projects –US Florida I-595, Poland A1 Phase II and Kenya Lake Turkana Wind Power – I have demonstrated some of the nuances of the current PPP market in the context of the global financial crisis. This brief analysis has shown an increased role for the public sector. The Florida project is the first availability payments scheme in the US and the public sector financing is a high percentage of overall project costs at 46 percent. The Poland project is completely financed by public institutions and its corollary project, the A2 required a sovereign guarantee to move

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forward. In Kenya, the public sector has increased its role from lender to Lead Mandated Arranger.

The increased role of the public sector is likely to continue and expand during the economic crisis, especially in the financial aspects of PPPs. These three examples represent the current trend and the market should expect projects with similar characteristics in the coming months.