# Multilateral Financing for Project Finance:

## Traditional Approach in Developing Countries vs. European Investment Bank ("EIB")

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# Traditional Approach

**Co-financing (A/B Loans)**

- A/B Loans have constituted the traditional means of multilateral support in developing countries
- B loans constitute direct financing of the commercial banks while A tranche has been funded directly by the multilateral banks either in USD or local currency
- By participating in the B tranche, commercial banks obtain the "umbrella effect" of multilateral participation by achieving the "preferred creditor" status

**Political risk insurance**

- Multilateral Investment Guarantee Agency ("MiGA"), a subsidiary of World Bank, has developed the issuance of political risk insurance whereby commercial banks are protected from: (i) convertibility risk; (ii) war and terrorism; (iii) expropriation; and, (iv) breach of contract
- While other multilateral banks, as well as private insurers, have equally participated in the political risk insurance risk, MIGA has been the key player in the market

**EIB approach**

- As an institution whose scope of activity has been focused in the European area, EIB has not been traditionally focused on the political risk
- EIB has focused of ensuring that project developer  benefit from the more advantageous conditions, in terms of pricing and tenors, on the back of its AAA rating
- Throughout the years, EIB has gradually taken more direct project risk by developing new financial products

# MIGA (World Bank) - Highlights

## What kind of risks are covered?

- Currency inconvertibility and transfer restriction
- Expropriation
- War, terrorism and civil disturbance
- Breach of contract
- Non-honoring or financial obligations

## Other benefits from MIGA insurance

- MIGA´s status as member of the WB Group: additional leverage in protecting investments
- Fast response to solve potential investment disputes, helping to keep revenues flowing
- Guarantees help investors to obtain project finance from banks and equity partners, though reduce risk-capital ratings
- Increase tenors: insurance coverage for up to 15 years (in some cases 20 if justified by the nature of the project) which may increase the tenor of loans

# IDB Group - Introduction

**The IDB Group is formed by**

Inter-American Development Bank (IDB), leading source of sovereign and non-sovereign guaranteed financing for social and economic development in Latam and Caribbean region

Inter-American Investment Corporation (IIC) focuses exclusively on the establishment, expansion and modernization of SMEs

Multilateral Investing Fund (MIF) works together private sector to develop, finance and execute innovative business models that benefit entrepreneurs and poor and low-income households

**IDB Group mandate**

The main mandate of the Bank is to foster the economic and social development of the IDB´s member countries, both individually and collectively

**Lending and Grants**

Through its different entities, IDG Group offers several financial products such as loans, grants and guarantees. The Bank´s lending and its grants are funded from four sources: *member countries subscriptions and contributions, borrowings from capital markets, equity accumulated and co-financing ventures*

# IADB Loans

## Public Sector Loans

Also known as Sovereign Guaranteed loans (SG)

•**Investment Loans**: Supports public and private sector investments projects

•**Policy-Based Loans**: Support institutional and policy changes on the sector or sub-sector level, through fast-disbursing funds

•**Emergency Loans**: Help countries cope with financial or economic crises or natural disasters

## Private Sector Loans

Also known as Non-Sovereign Guaranteed loans (SG)
•**A/B Loans & Syndications**:IDB can work together banks and institutional investors to co-finance private sector projects

•**SMEs**: Designed to provide financing to broaden the participation of entrepreneurs in their local economies

•**Opportunities for the Majority Initiative:** Finances market-based sustainable business models that engage private sector companies, local governments and communities in the development and delivery of quality products and services

Multilateral Support for Project Finance

# IDB Guarantees

## Public Sector Guarantees (Sovereign)

IDB has a Guarantee Disbursement Loan Program that provides the option of disbursing loans in the form of a guarantee

This allows the borrower to take all or a portion of a loan disbursement in the form of a guarantee and use it to enhace the terms of borrowing from private sector sources:

•Extending tenor
•Reducing interest rates
•Increasing borrowing capacity

## Private Sector Guarantees (Non-Sovereign)

IDB Guarantees are also available to private business or subnational entities without a government guarantee

•**Credit Guarantees**: IDB coverage for all risks for selected terms of a loan made by a commercial lender. Guarantees cannot exceed 25% of total project costs, or USD 200 mll, whichever is lower.
•**Political Risk Guarantees**: Guarantees for debt instruments: breach of contract guarantees, currency convertibility and transferability guarantee and other political risks. Coverage extends up to 50% of project costs or USD 150 mll, whichever is less

EIB project Finance Credit Enhancement

# Highlights of programme

## Amount

- €235 mm allocated under the 2007-2013 budget
- Up to €4 billion of financing expected to be raised

## Timeline

- Pilot Phase already launched for transaction to be closed by 2016
- 8 transactions approved under the Pilot scheme
- So far only €1.4 bn Castor project in Spain while the A-11 project in Belgium is expected to issue bonds in the coming months

## Sector

- Projects need to have a trans-european nature
- Belonging to either transport, energy or information/communicatio n industries
- Projects need to have a construction element. Pure refinancings not eligible

## Form

- Either as a contingent guarantee or on a subordinated form
- For up to 20 % of total debt up to 390 % could be considered as an exception)
- If issued as contingent guarantee, it would cover all risks, including construction, as well as accelerated payments.
- Target: raising the rating of the project from low IG to up to A rating

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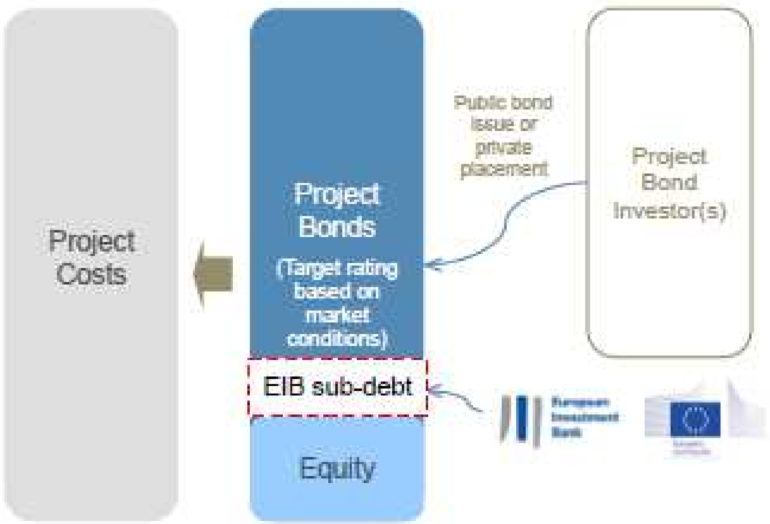
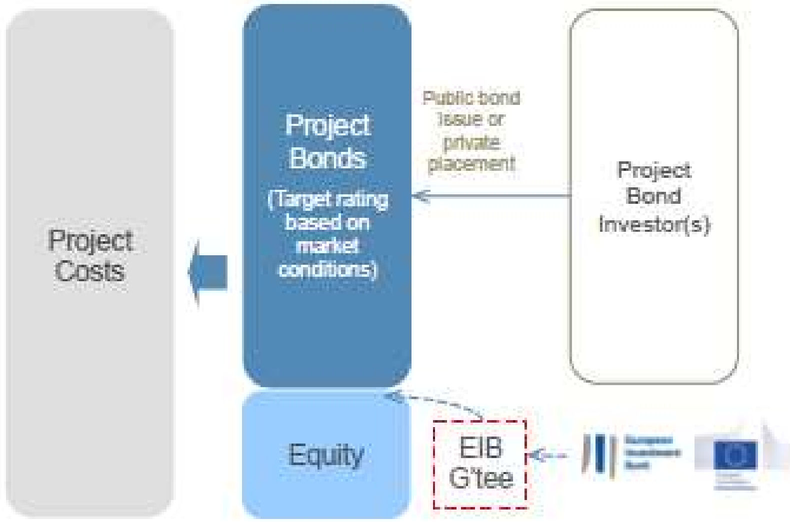
EIB Project Finance Credit Enhancement

# Credit Enhancement Scheme

**Funded (Subordinated) Guarantee**




**Unfunded/Contingent Scheme**



# Watercraft Capital (Castor): brief asset description

2013 Spain

EUR 1,434,000,000

## Asset Description

- Gas storage facility close to Valencia with capacity for up to 1.3 bcm of useful gas
- Facility to be included in the Spanish Gas system and therefore, to be remunerated, as per the applicable regulation by the end user.
- Award date: 2008
- Concession life: 30 year (extendable twice for a 10 year period)
- Remuneration to be received regardless of actual use of the facility
- Regulator: Comisión Nacional de la Energía
- Consortium:
  - ACS
  - Enagas
  - Dundee Energy Ltd.

## Banks

- Bankia, BNP Paribas, CaixaBank, Credit Agricole CIB, Natixis, Santander and Société Générale

## Debt Structure & preliminary Rating

- Total Debt: € 1,434 mm
- Final maturity Dec. 2034
- Average life: 12 years
- Security:
  - EIB PBCE: €200 mm
  - Shareholder L/C equal to 5 % of Bonds
  - 6 month debt service reserve
- Rating
  - BBB by S&P and BBB + by Fitch
  - one notch above Spanish sovereign rating

## Timeline

- Award of Concession in 2008
- Original financial Close in June 2010
- Bond refinancing closed in July 2013

# Strengths and Challenges

**EIB credit enhancement programme shows the pan-european commitment level for the development of infrastructure**

**The product may be hampered by the complexity of the structure which may limit its application to a handful of projects**

## Strengths

- Rating upgrade will widen potential investor universe
- EIB participation constitutes a “seal of approval” smoothing investor approval
- Unconditional, irrevocable guarantee covering any credit event.
- Helps kick-start European Project Bond market

## Challenges

- The guarantee is limited to 20 %, or at best 30 %, so that project risk is reduced but not eliminated
- Only applies to project with a tran-european content
- The product can only be applied to projects which have not achieved construction completion
- Inter-creditor issues remain a stumbling block
- Not applicable to private placements

# Other means of support

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|---|---|
| **Loan Guarantee Instrument** | • Also known as LGTT, is a special instrument develop jointly by the EIB and the EC to facilitate private sector involvement in core European transport project on a 4real toll basis.<br>• In the form of a stand by liquidity facility guarantee by EIB, it supports, with up to 10 % of the project, the ramp-up (up o 5 operating years) period of Greenfield projects in case they find unexpected traffic reductions. |
| **Intermediated Loans** | • EIB provides direct funding to financial intermediary institutions funding projects which "…increase growth and employment potential… …promote economic cohesion… linking regional and national transport infrastructure".<br>• Intermediary institution retains all risks (there is no direct relation with ultimate borrower) nut the former needs to transfer the financial advantage derived from EIB loan |
| **Miscellaneous** | • Apart from traditional direct project finance lending (up to 50 %, pari-passu, fully secured…) the EIB continues to develop other financial instruments to help the development of infrastructure project of all sizes (Urban Development, Jessica; Sustainable Energy, ELENA….) but its impact is more limited due to the scale of the projects involved |