

Project Finance Security Structures - Case Studies in the Energy Sector



June 5th, 2014



Section I: Security Structure and Case Study

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About China Exim...

- ❖ Established in 1994
- ❖ Credit ratings are compatible to the national sovereign ratings

	 中国主权 China's Sovereign Ratings	 中国进出口银行 THE EXPORT-IMPORT BANK OF CHINA
STANDARD & POOR'S 美国标准普尔公司	AA-	AA-
 美国穆迪投资者服务公司 Moody's Investors Service	Aa3	Aa3
惠誉信用评级有限公司 Fitch Ratings	A+	A+

- ❖ Branches & Rep. Offices
 - Domestic: 21 business branches
 - Overseas: 1 branch in France, 2 Rep offices Russia and South Africa
 - Rep. office in France going to be promoted to the 1st oversea branch

What's special about us...

❖ Core competitiveness

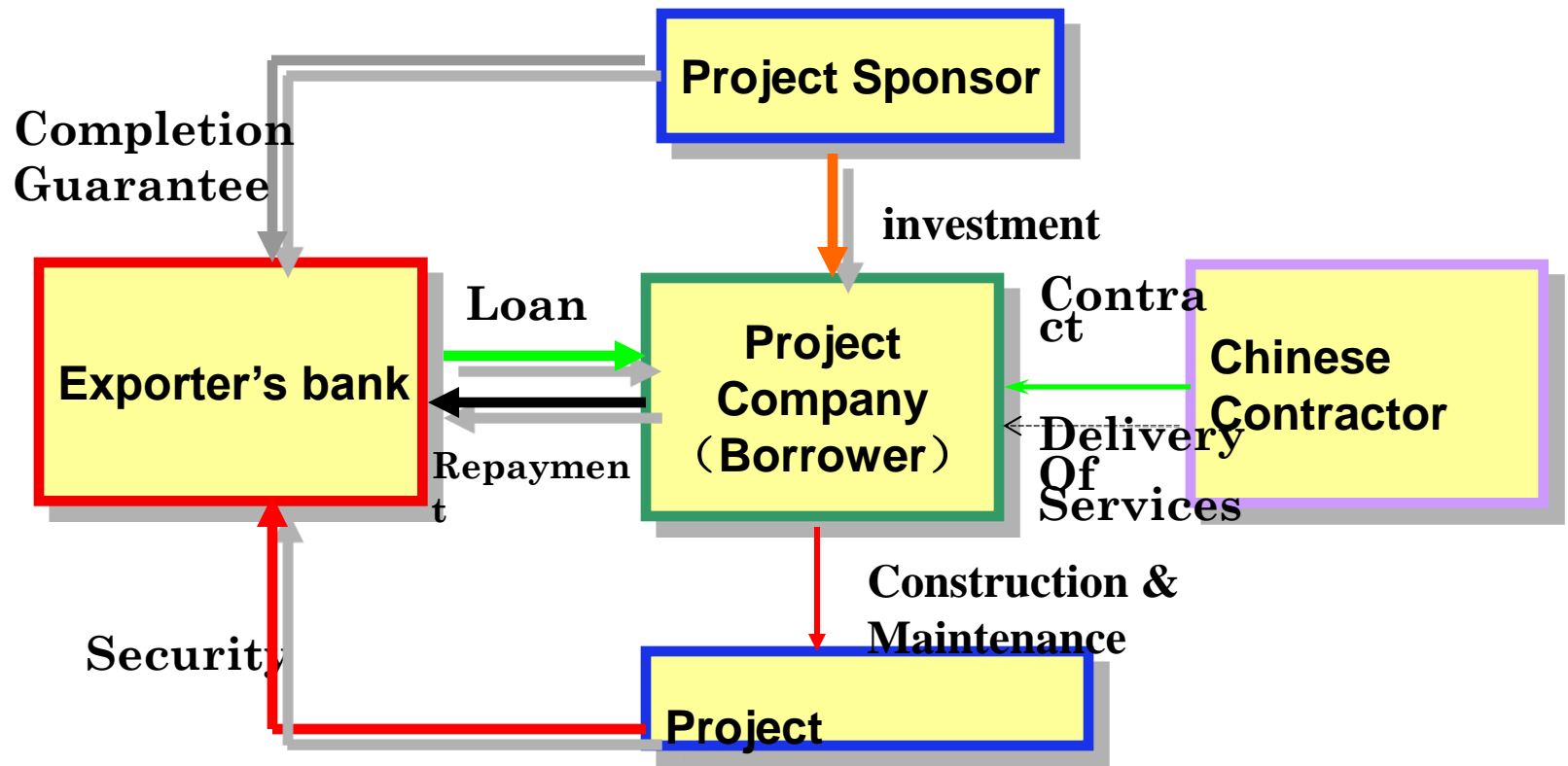
- Highest rating among Chinese banks
- Oversea business ties with local governments and leading companies over 140 countries
- Long-term relationship with Chinese government and supervisory authorities
- The only undertaker of Chinese concessional loans
- Ultra long loan tenor and competitive interest rate
- Tailor-made financing products
- Professional teams in oversea projects

Project Finance-Definition

The financing of long-term infrastructure, industrial projects and public services based upon a non-recourse or limited recourse financial structure where project debt and equity used to finance the project are paid back from the cashflow generated by the project.

- ❖ **project financing is a loan structure that relies primarily on the project's cash flow for repayment, with the project's assets, rights, and interests held as secondary security or collateral. Project finance is especially attractive to the private sector because they can fund major projects off balance sheet.**

Project Finance Structure



Case Study 1

❖ **Project Overview**

The project is a typical case of project financing. The owner is a wholly owned subsidiary of a leading investor-operator in the Asia Pacific energy sector. The power plant involves a 1,320 MW (2 x 660 MW) domestic coal based power project , located in India. The EPC contractor is a Chinese company and the total contract value is about 1 billion US dollar. The Equity-Debt Ratio is 35:65 and the financing amount is approximately 0.8 billion US dollar which includes local rupee loans and international US dollar loans. The 25-year PPA was executed with two local electricity companies. The 25-year Fuel Supply Agreement was executed with domestic coal company and cost of coal was a complete pass-through in tariff.

Case Study 1

❖ ***Project Documents***

- ❖ Loan Agreement
- ❖ Security Agent Agreement
- ❖ Sponsor Support Agreement
- ❖ Share Pledge Agreement
- ❖ Indenture of Mortgage
- ❖ Trust and Retention Account Agreement
- ❖ Letter of Guarantee by the EPC contractor
- ❖ Consents to Assignments
- ❖ The Director's Declaration
- ❖ The Memorandum of Hypothecation



Case Study 1

❖ *Risks and Mitigates*

Risks	Mitigates
Technical	External Adviser's Pre-feasibility study, EPC contractor's feasibility study, Lender's independent adviser Lahmeyer's review
Environment	ERM as the independent adviser, passed through the Equator Principles, India government's approval
Fuel supply	25-year Fuel Supply Agreement with local coal company, Grade 'E' coal with low ash and sulphur, permit of blending imported coal
Off taker	Local electricity companies- LC issued by local banks
Political	Political insurance policy by Sinasure

Case Study 1

❖ *Risks and Mitigates*

Risks	Mitigates
Market & Price	CRISIL as the Lender's independent market adviser, cost of coal was pass-through in tariff, assignment of PPA to Lender
O & M	Experienced team in similar projects
Construction and Completion	Track record contractor, Letter of Guarantee by the contractor, the committee of cost overrun by the sponsor
Exchange rate	The US loan was hedged by the borrower
Conflicts with other lenders	Representations and Warranties in the Loan Agreement

Case Study 1

❖ Question 1:

❖ **What are the industries suitable for Project Finance?**

Case Study 1

❖ Question 2:

- ❖ **What are the requirements for the sponsor? Shall they provide completion guarantee?**

Case Study 1

- ❖ **Question 3:**
- ❖ **Can we finance a power plant by Project Finance without PPA or fuel agreement?**



Section II: Take security in local law environment

Background

- ❖ Generally speaking, English law is more predictable
- ❖ English law is more comprehensive, it support nearly all security
- ❖ But take security you must comply with the local law
- ❖ Some security may not be supported in developing countries
- ❖ Solution based on experience, not rules

Purpose of taking security in project finance

Low liquidity

High liquidity

Security Assets of Project Finance

Security Assets of Simple Property Development



中国进出口银行

THE EXPORT-IMPORT Company name

Purpose of taking security in project finance

- ❖ 1. Defensive: ranks ahead of the general unsecured creditors, keep the project operate in a way maximize the interest of the security lenders.
- ❖ 2. Offensive: if the borrower doesn't do well in running the project, then...
- ❖ 3. Management: Cash flow management
- ❖ 4. Exercise the lenders' right without third party consents.

Suboptimal Solution In Taking Security



Security on license or right can't be transferred



Insurance and reinsurance

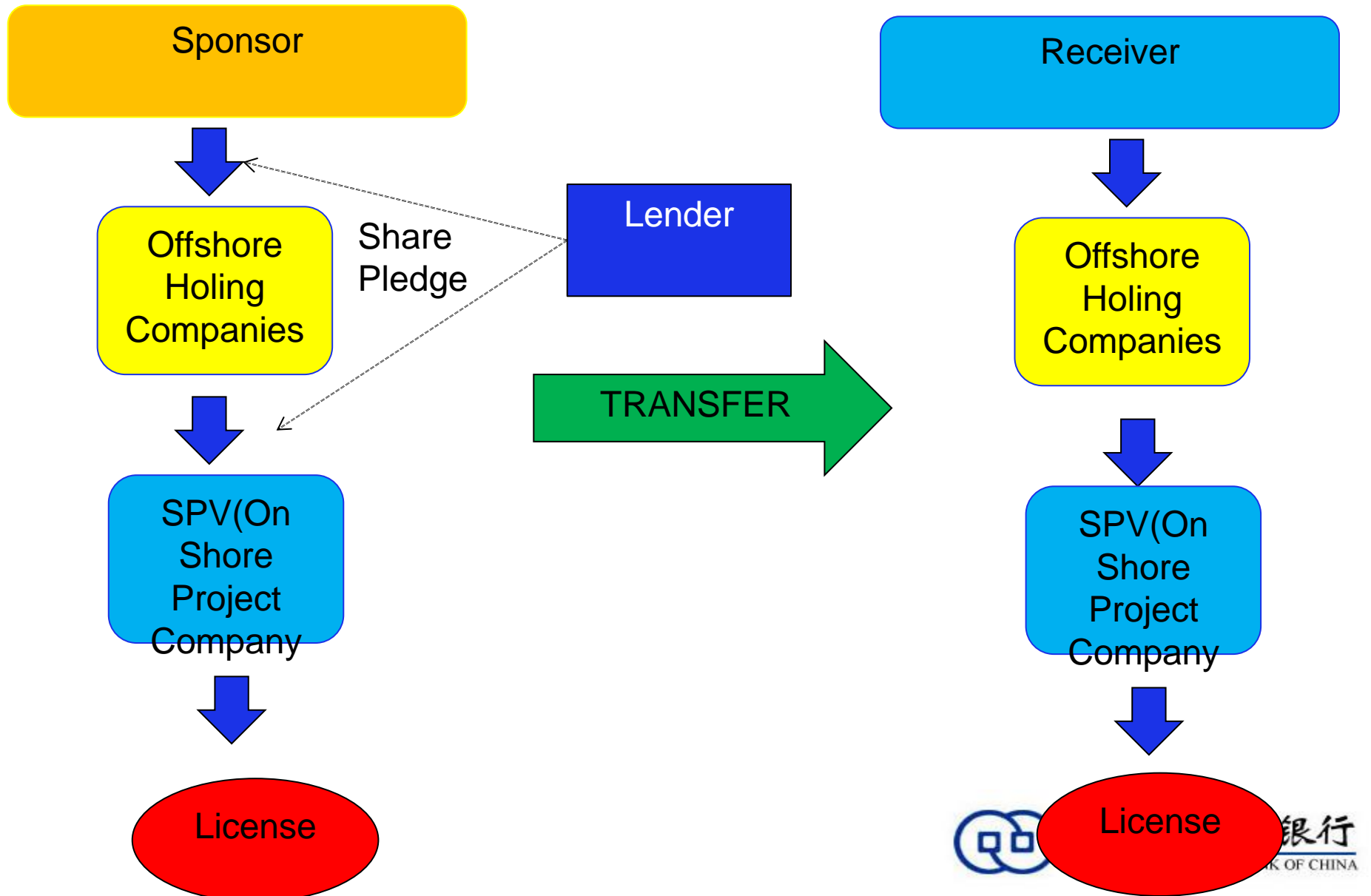


Direct agreement



Account management

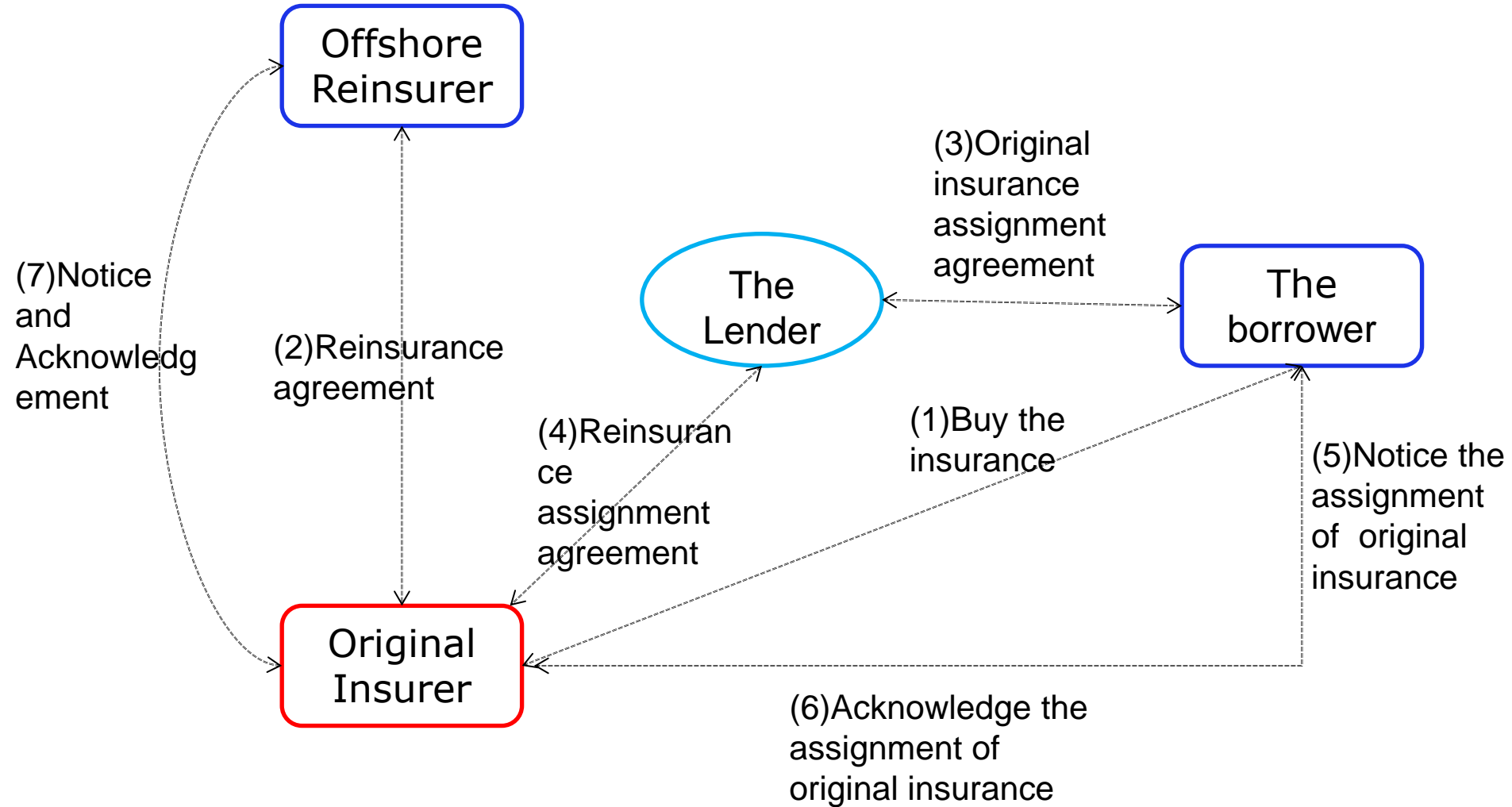
License Or Right Can't Be Transferred



Insurance and Reinsurance

- ❖ Local insurance company issue requirement :5% to 20%
- ❖ Buy the commercial insurance from the local insurance company
- ❖ Reinsurance: original insurer's credit rating is not satisfied by the lender. Major player in global insurance market should be the reinsurer and bear most of the risk.

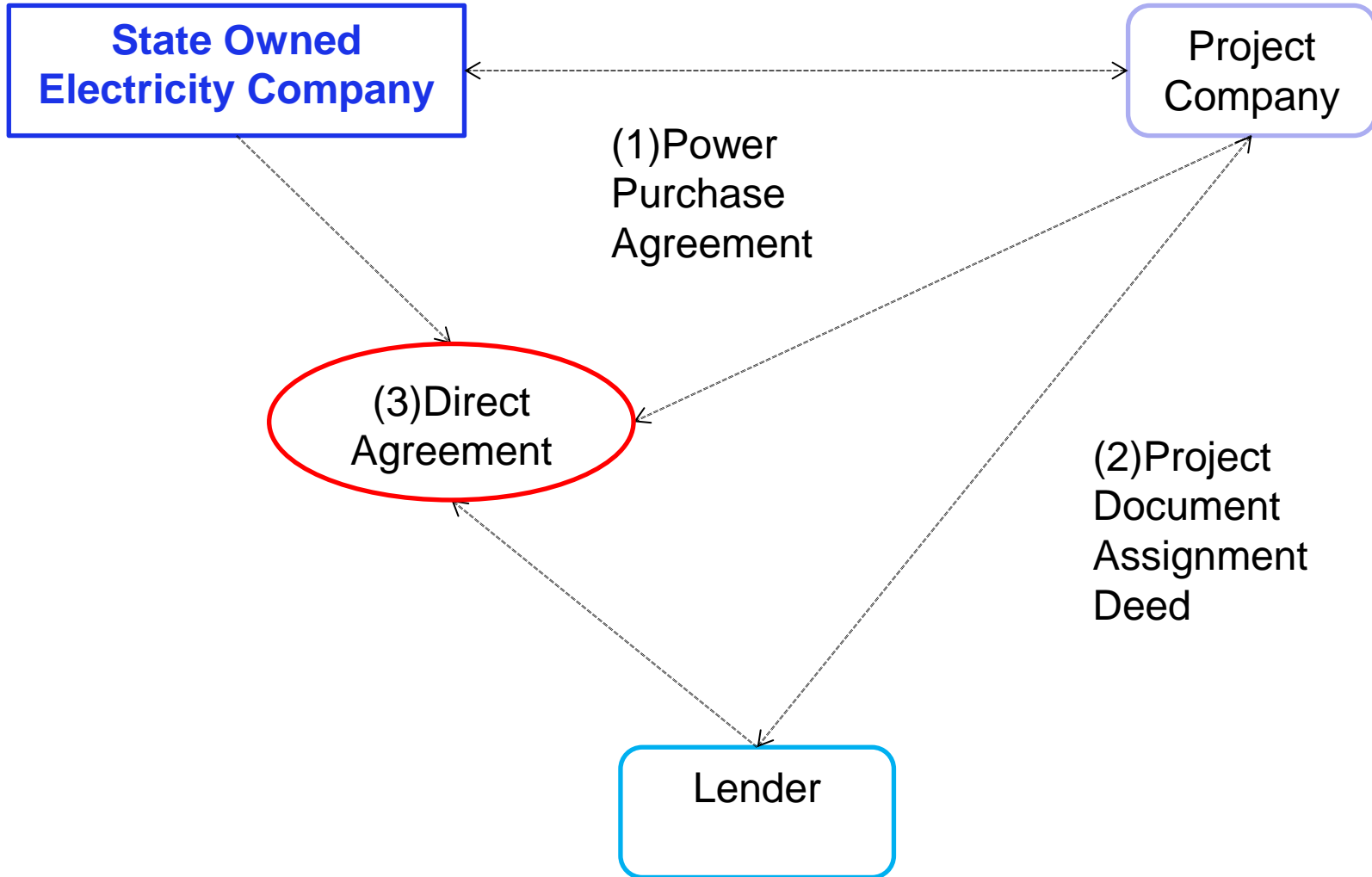
Insurance and Reinsurance



Direct Agreement

- ❖ Parties of direct agreement: (1) the project company;(2)lenders;(3)Parties to the project's key underlying commercial contracts
- ❖ Objects: both defensive and offensive, to enable the lenders to “step into the shoes” of the project company if the borrower default.(step in rights)
- ❖ Key underlying commercial contracts:
Concession agreement, PPA, EPC, SPA etc.

Direct Agreement



Direct Agreement-Negotiation Focus

Notice and Acknowledgment

- Consent from the key contract party that the project company can assign its rights under the project document to the lenders.

Avoid Termination

- The contract party will not terminate the project agreement without first giving the lenders a specific number of days' prior written notice.

Step in right

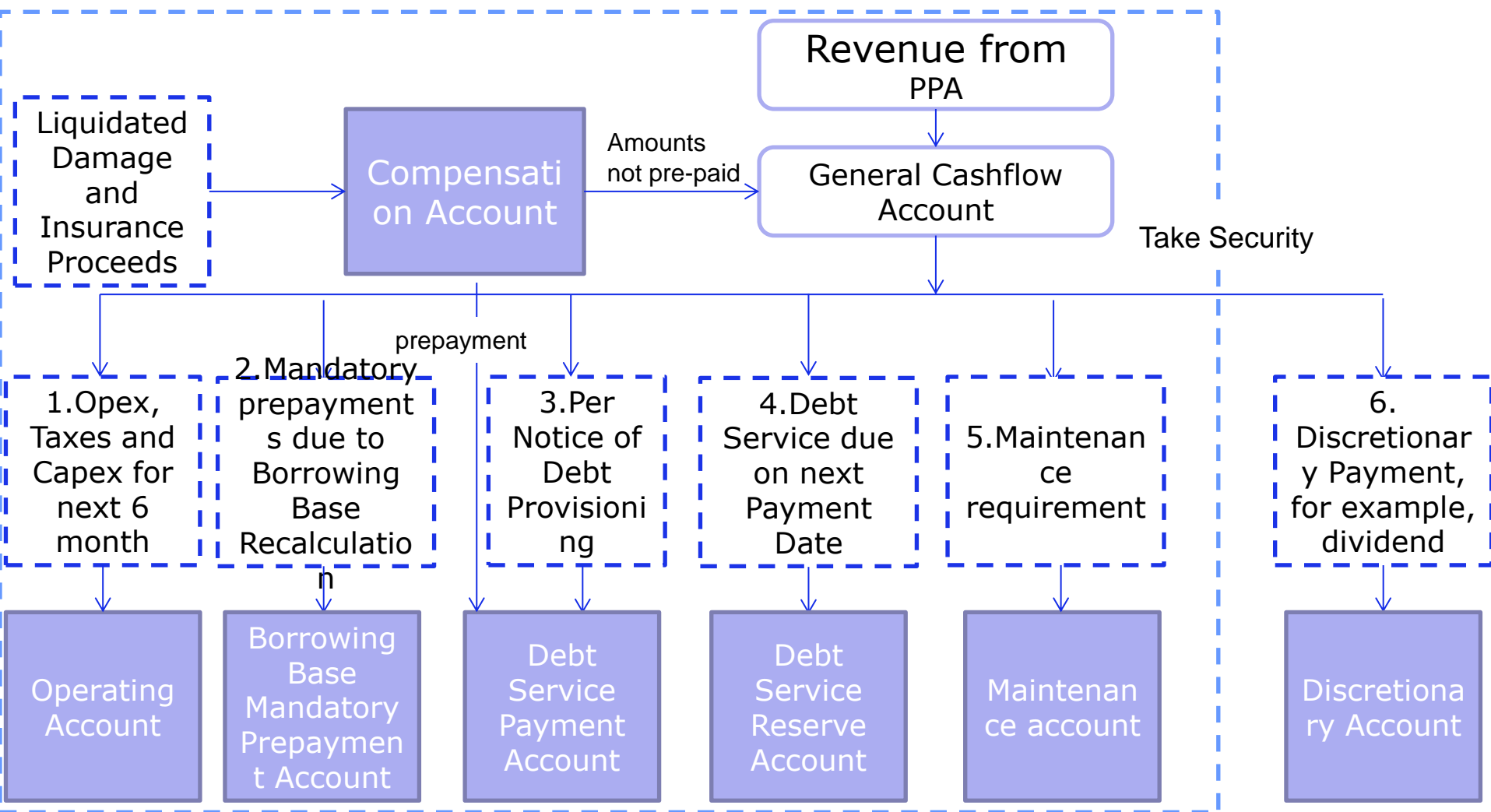
- Upon the notice of lenders, the contract party agree that lenders themselves or receiver can step in the project. And the project document will still be valid.



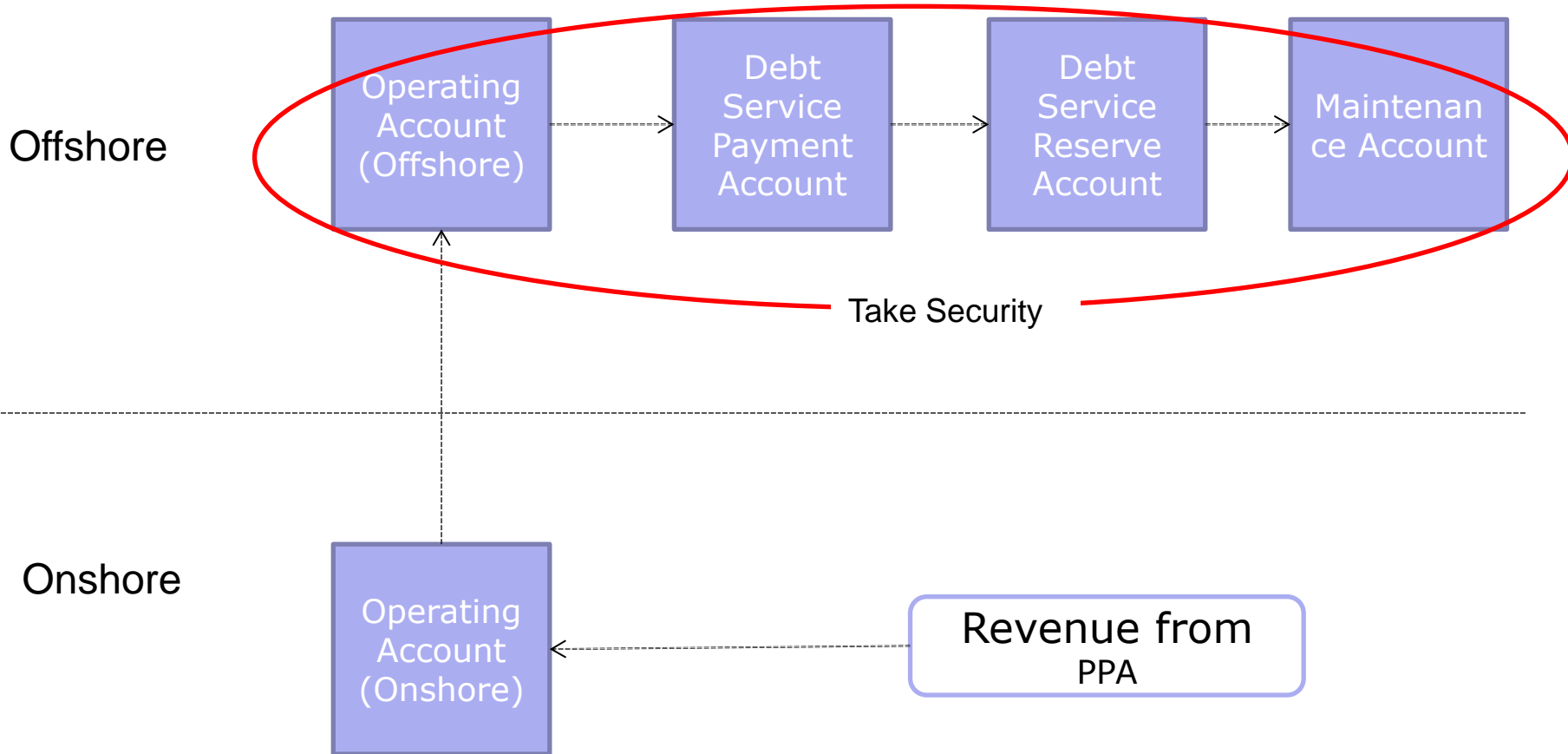
Direct Agreement-Further discussion

- ❖ EPC Contract DA consideration: The strength of sponsor support, LNG project
- ❖ Concession agreement DA consideration: (1) highly regulated industry requirement; (2) the lender may compromise on the step in right, for example, the authority can decide whether the receiver is qualified.

Account Management- Typical Cash flow Waterfall



Account Management-Only take security of offshore account



Account agreement:
cash sweep onshore
cash flow to offshore
account immediately



Thank You !



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We are looking forward to our cooperation in the near future

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in a better world?*

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