



# Project financing

## Introduction

Conventional export credit financing involves financing where the borrower or guarantor is creditworthy in their own right. Where this is not the case, perhaps because the borrower is a new company, or the country has limited hard currency, a structured financing with features mitigating the risks may be possible.

This section describes how ECGD is currently handling structured financings, including Limited Recourse Project Financing, Structured Corporate Financing and the Foreign Exchange Earning Projects.

## Project Financing Scheme

Project Financing is the term used to describe the financing of a major new project or large project expansion when the lenders place primary reliance on the revenues of the new project for repayment, as well as using the assets and contracts of the project as security. The project owners are usually responsible for ensuring that the project is built and operated successfully, taking responsibility for making up any shortfall in the project's earnings in only limited, clearly defined circumstances. Other terms used to describe these arrangements include limited recourse and Build-Own-Operate-Transfer (BOOT) schemes, although there are many variants on this theme.

Our Project Financing Scheme aims to help UK exporters win business by operating in a flexible, responsive and cost-effective way to meet the needs of all the parties involved. Many bankers and sponsors have already found that ECGD involvement can bring forward additional funding to this type of project. Owing to their complexity, some project financing cases may take a number of years to complete and entail considerable expense. It is nearly always quicker, where such a possibility exists, to set up financing arrangements on a more conventional basis with the backing of a creditworthy borrower.

## Benefits of ECGD Support

### For the exporter

The exporter will normally receive payment from an ECGD supported loan shortly after the goods are shipped or services are performed. There will also be provision to finance an arbitration or termination settlement from the ECGD supported loan.



## For the bankers

ECGD normally guarantees the financing bank 100 per cent of the loan value and interest payable from the date of loan effectiveness. Some other export credit agencies provide only up to 95 per cent guarantees. There are two forms of cover available to lenders under the scheme:

- All Risks Cover - ECGD can provide up to 100 per cent guarantee against losses arising from both political and commercial events. The guaranteed loan can fund up to 85 per cent of UK content and eligible foreign costs. If any principal instalment or interest due under the loan is not paid in full, ECGD pays the bank 90 days after the date on which the payment was due. ECGD will also pay interest on the defaulted amount for the 90 days the bank has to wait for its payments.
- Political Risk Cover - this also provides cover for the principal and interest value of a loan financing up to 85 per cent of the contract value, but protects the lenders only against non-payment directly attributable to political causes of loss, to be specified at the outset. The risks are established on a case by case basis but typically may include the following country risks:
  - War, civil war, rebellion;
  - Prevention of, or delay in, the payment of external debt by the host government or by that of a third country through which payment must be made;
  - Cancellation or non-renewal of an export licence;
  - Expropriation where the host government is not a shareholder in the project.

Failure by a host government to honour written obligations in respect of the project can also be considered, provided such failure causes a loan default and is not itself brought about by any action or inaction of one or more of the other parties to the project.

## For the project sponsors

ECGD may be able to provide interest rate support to banks so that loans given to the project sponsors will attract officially supported fixed rates of interest. Alternatively, cover for contracts financed can be at commercial floating or fixed interest rates. Loans can also be offered in a range of currencies, including, in a number of countries, the local currency. Officially supported fixed rates of interest and the length of credit available to sponsors are determined in accordance with the OECD Arrangement on Export Credits.



## **Costs**

### **Premium and other charges**

Premium will be payable at the time the ECGD documents are signed and includes a non-refundable administrative charge which is set case by case. Rates will also be calculated on a case-by-case basis in the same way as for other ECGD business. In addition, any external costs we incur will be charged as fees to the applicant or project sponsor as they are incurred. This includes the costs of any independent advice commissioned by us, for example, those involved in the project appraisal, the procurement of external legal advice, and any travel and subsistence expenses incurred.

### **What ECGD will be looking for;**

ECGD seeks to operate a flexible scheme with as few ground rules as possible. Each proposed transaction is considered individually with our requirements being similar to those which any other party taking senior lending risk in the project would be exposed.

### **Eligible projects**

ECGD support can be considered for any projects which are likely to be viable, and where the project financing technique is capable of being satisfactorily applied and negotiated with appropriate parties capable of sharing the risks. Given the significant administration costs involved, only projects with an ECGD supported loan of at least £20 million will normally be considered.

Only under exceptional circumstances can a lower value loan be considered both in terms of where there is a compelling reason for ECGD support and where ECGD costs can be minimised to its satisfaction.

### **An acceptable risk**

There is no precise formula for defining an acceptable risk. Each case will have to be judged on its own merits. Nevertheless the following indicators of acceptability will as a minimum always apply:

- International commercial bank finance should be available on the same security as that offered on the ECGD-backed finance;
- The individual performance and financial obligations of all the parties to the project, including the host government, the sponsors, contractors, suppliers, operators and buyers of the product involved must be regarded as acceptable by us;
- An independent appraisal of the validity of the assumptions in the feasibility study must confirm a reasonable assurance of timely payment of amounts due to the senior lenders.

Other factors that we would regard as helpful would include the following:

- Development finance institutions (such as the International Finance Corporation or the Commonwealth Development Corporation) with investment grade ratings or of a similar standard supporting the lending on the same security;
- The project being given a preliminary investment grade rating by Standard & Poors, Moodys, or other acceptable rating agency.

### **Risk sharing**

Risk sharing will be a requirement of ECGD support for all projects. It is normal commercial practice for the risks to be allocated to the parties best suited to manage and influence those risks but ECGD recognises that this is, essentially, a matter for negotiation.

### **Limited Recourse**

The project financing facility allows for only limited recourse to the project sponsors. ECGD will expect the lenders to retain the right to take recourse to the sponsors, and others whose involvement is necessary to the success of the project, in limited but clearly defined circumstances and amounts. ECGD will agree the extent of recourse to each party depending on the circumstances of the case, taking into account the views of the various lenders. For example, recourse might be taken to sponsors in the sense that they may be providing standby equity for cost overruns or to the host government to the extent that it has provided a legally enforceable non-interference undertaking coupled with a financial indemnity. The lending supported by ECGD will rank as senior debt, *pari passu* with other senior debt.

### **Risk analysis and security**

It is generally recognised that processing project financing cases can be resource intensive and requires specialist skills. To appraise and to identify the acceptable level of risk to remain within the project company and which risk can reasonably be transferred outside that company to others is a complicated and detailed process. This involves the lenders negotiating an acceptable security package for the project with other participants and ensuring this is duly reflected in both the financial structure and project documentation.

Since we will not provide All Risks cover without some co-financing ECGD recognises that the development of an acceptable package is a joint activity involving all participants, each with their own concerns and responsibilities.

### **Procedures**

There are, broadly, three main stages in getting our support under the Project Financing Scheme. The first is the Initial Enquiry, the second is the Proposal and Negotiation Stage and the third is the Signing of the Documentation. The purpose of each stage, the information required and the response, which you can expect from us, are set out below.



## **Initial Enquiry**

ECGD recognises that embarking upon a project financing facility is challenging, complicated and time consuming. To help the exporters, bankers or project sponsors get on the right road with us we will be pleased to have initial discussions to gauge what might be feasible. You should contact the relevant underwriter.

## **Proposal and Negotiation Stage**

ECGD's approach is to process project financing cases as quickly and efficiently as the major banks, by forming a project finance case processing team at the initial negotiation stage led by an underwriter and comprising a financial analyst from its Operational Research Services, a legal adviser from its General Counsel's Office and other internal experts, if appropriate. At a later stage, in addition to external legal advisers, other external technical or financial experts may join the team.

## **Your Proposal**

First, you should provide ECGD with at least the following:

- A brief description of the project;
- A brief description of the sponsors and shareholders, including extent of host government involvement;
- The overall cost and structure of the project;
- The likely UK content in the project and UK export credit loan value required;
- A proposed financing plan, setting out the forms and details of finance envisaged and proposed financiers, including export credit agencies and international commercial banks;
- The cover option required (All Risks or Political Risk only);
- The repayment terms required;
- An outline of the security package;
- Feasibility studies;
- Any cashflow projections with scenarios/sensitivity analysis;
- A description of what additional information is being obtained;
- A list of agreements envisaged and their status.

## **Our Indication**

ECGD will then be able to respond by indicating, but without any form of commitment:

- Whether the amount of support requested for the project is in principle acceptable;
- The likely repayment terms ECGD can agree, (subject to carrying out the OECD international notifications procedure);
- The current interest rates (if interest rate support is sought);
- The likely ECGD premium rate;
- Its approach to evaluating the likely risks and security requirements (which will depend on the cover option requested);
- Any other information required.
- The indication will be subject to the project in its totality being fully assessed and analysed as an acceptable risk when we have all the information we require.

The purpose of this early written indication is to enable you to:

- Identify the various steps which have to be taken, by whom they will be taken and when;
- Understand ECGD's requirements and plan ahead to meet them expeditiously.

## **Detailed assessment and due diligence**

Before giving our approval ECGD will need to review:

- The terms of all contractual arrangements for the project (for example concession, supply or off-take agreements);
- The independent appraisal work undertaken on behalf of the various lenders and export credit agencies;
- The spreadsheet model to carry out additional scenario analysis;
- Project information memorandum prepared by the sponsors and the proposed term sheet;
- The proposed financing arrangements.



## **Appointment of external consultants**

ECGD may want to be satisfied that the project proposals have been subjected to a rigorous independent appraisal. This could be done by or on behalf of a respected international commercial bank, a development bank, another export credit agency or another financial institution, so long as they are providing or guaranteeing finance for their own account and further that ECGD has access to the findings, so as to enable ECGD to make its own judgement.

If such an appraisal is not available or has not been done to ECGD's satisfaction, then ECGD may commission its own studies, if necessary using external consultants, who will be managed by ECGD and whose costs will have to be borne by the applicant/project sponsor.

ECGD may be willing, under the right conditions, to share our external consultant with other export credit agencies in order to keep costs to a minimum.

## **External legal advice**

ECGD will require an opinion on the documentation from an external law firm independent from the firm employed as legal adviser to the banker/lenders, as our interests are not always identical to the interests of the banker/lenders. Once again ECGD may be willing, under the right conditions, to share its legal adviser with other export credit agencies in order to keep costs to a minimum.

## **Approval**

In giving its approval ECGD will issue a letter of intent setting out the terms of support, which will be provided. This letter will be subject to a number of conditions, which are likely to include amongst other things completion of any due diligence still outstanding and the preparation of satisfactory documentation.

## **Signing of documentation**

ECGD documentation (the ECGD-supported loan agreement, our guarantee to the banks and a premium agreement with the exporter) will be signed when all the parties have reached agreement on the basis for the project to proceed and all the relevant agreements or contracts are signed or close to being signed. The documentation will set out conditions precedent to be fulfilled before ECGD support is finally effective. These will pick up any loose ends and ensure that all the parties to the project are fully committed before any money is advanced.

## **What next?**

ECGD believes that its approach to Project Financing is flexible and responsive and can meet the needs of well thought-out projects where the risks are acceptable to ECGD. ECGD's aim is to help UK exporters and investors to win business.

Should you require any further general information on the scheme or if you have a specific piece of business in mind, ECGD's underwriters will be pleased to discuss your proposals.

## **Structured Corporate Financing**

There may be cases where the country repayment risk is not a constraint, but a pledge of dedicated hard currency revenues from an existing investment can be provided to lenders as security in order to improve the creditworthiness of a particular borrower. There may also be covenants available, which adequately protect lenders against a financial deterioration. In these circumstances ECGD is normally willing to consider propositions, which involve an element of risk sharing between ECGD and the export credit lenders.

If you have a particular case please contact the relevant underwriter.

## **How ECGD might be able to help further**

### **Overseas Investment Insurance**

ECGD has another scheme, which is designed to encourage investment flows overseas. It can be used in addition to the facilities outlined above. UK investors and lenders can use ECGD's Overseas Investment Insurance Scheme to protect equity and/or loan investment against the political risks. There is no requirement that the funds being insured must be used to finance UK exports and, indeed, loans must be untied from the supply of goods or services.

Taking out investment insurance in no way affects the amount of export credit support available. For more information please telephone our Overseas Investment Insurance Branch on (+44) (0) 20 7512 7767, or email: [oii@ecgd.gsi.gov.uk](mailto:oii@ecgd.gsi.gov.uk)