

FINANCING INFRASTRUCTURE PROJECTS

Trans-Asian Railway Course

BIMSTEC & MGC Railway Officers

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Infrastructure Project Characteristics

- Traditionally Government funded
- Normally for public utilisation
- Impact socio-economic environment
- Capital Intensive and Long gestation period
- Assets have long life
- Either '*Open Access*' or '*Limited Access*'
Services

Trans-Asian Railway

- Many countries to build new and missing lines
- Interoperability may require investments in rolling stock, locomotives, common maintenance facilities, signalling etc
- Every country may not find required resources on priority
- Non-government funding therefore becomes essential for implementation – *public private participation (PPP), Build operate Transfer (BOT), Build Own Operate Transfer (BOOT), Build Own Operate (BOO), Build Own Lease Transfer (BOLT) etc*

Benefits of Public Private Partnership?

- Reduces Government's funding
- Private enterprise able to reduce project cost through better and faster implementation
- Government risk reduces
- Government support and private enterprise provide synergy to project
- Better service to public as specialisation becomes available

Special Purpose Vehicle (SPV)

- Company set up for specific purpose
- Promoted and supported by principal stakeholders
- Part financing by ‘market borrowings’ – debt: equity ratio important
- Options for operation and maintenance
- Fair and just Concession a pre requisite

Benefits to SPV by Government Participation

- Easier availability of land, approvals, clearances etc
- Signal of support to lenders
- Greater the support easier the finance raising and terms

Steps – Project Development

- Determine scope of project & Engineering, Procurement and Construction (EPC) cost
- Determine other expenses: Development costs, Financing costs, costs to mitigate Environment & Social impact etc.
- Assess total ‘Traffic’
- Determine Operation & Maintenance (O&M) costs
- Risk & Mitigation Plan
- Project cash flows through concession period
- Financial analysis –most efficient financing method

Financing Methods

- SPV
- Concession
- Leasing
- Securitisation

Due Diligence - Risks

1. Project Completion Risk

- Design & Construction Risk
- Cost & Time Overrun Risk
- Financing Risk

2. Market Risk

- Volume & Price Risk
- Payment Risk

Due Diligence - Risks

3. Operating Risk

- Performance Risk
- Maintenance Risk

4. Regulatory / Political Risk

- Change in law or Political Force Majeure

5. Force Majeure Risk

- Events outside control of borrower / lender

Evolution of Project Financing

- *Earlier*
 - Largely based on sponsors' strengths
 - Limited structuring
 - Sometimes sponsors did not meet commitments
- *Now*
 - Based on future cash flows as main source of debt servicing
 - Structured for risk mitigation
 - Focus on project architecture

Structuring Characteristics of Infrastructure Projects

- ‘Willingness’ to Pay by user is important
- Normally implemented when critical
- Natural growth of Demand likely
- Facility designed to provide sufficient spare capacity – usage low initially
- Debt: Equity ratio; Debt Service Coverage Ratio important criteria

Financial Structuring

- Is process of *Managing Financial Risk* and *Building Consensus Amongst Stakeholders*:
 - Balancing risk profiles of participants
 - Suit expectations of parties on investments
 - Principle of higher reward for higher risk applies
 - Covers estimated cash flows, gearing, available financing, terms of finances and risk appetite
 - Preferably project debt and equity paid back from cash flows generated by project

Sources of Finance

- Speciality Funds – equity funding
- Debt Finance
 - Long term debt from international markets
 - Developmental Financial Institutions
 - Commercial banks
 - Multilateral Institutions
 - Export Credit Agencies

Other Options of Funding

- Bonds :
 - Taxable
 - Tax Free (where permitted)
- Discount offers to beneficiaries in user rates
- Gap Funding by Government
- Local Government grants

More Funding sources

- Pension funds, Provident funds
- Insurance funds
- Trust Funds

These look for safe investments, less risk and assured regular return over extended periods – ideally suited for infrastructure projects – tax incentives also available

HARD TRUTH - INFRASTRUCTURE PROJECTS

- No matter what financing is done or who are the investors or what is the shareholding pattern –

***THE GOVERNMENT IS
ULTIMATELY RESPONSIBLE
FOR THE ASSET***

Thank You for your attention

On behalf of AITD I wish all
participants a pleasant stay and fond
memories of their visit to India