

Commercial Cofinancing and Credit Enhancements

Orientation Program for
DMC Officials
October 21, 2008

Agenda

- ADB Financing Instruments
- Why Commercial Financing
- What are Credit Enhancements
- Guarantees
- Syndications

ADB Financing Instruments

- Equity
- Loans for sovereign and non-sovereign projects
- Grants and Technical Assistance
- Credit Enhancements

Why Commercial Cofinancing?

- The Asia-Pacific Region requires over \$470 billion of investment in infrastructure each year over the next 10 years
- DMC governments, donors, and ADB, can finance only a portion of the amount of investment required
- The financing gap will have to be filled by commercial lenders

Constraints Affecting Commercial Lenders in DMCs

- Political risks continue to be ranked as a main constraint to the flow of FDI in DMCs
- Private investment in infrastructure is perceived as high risk, especially when it comes to regulatory and contractual risks
- New banking regulations under Basel II make lending to projects in some DMCs prohibitively expensive
 - Loan provisions can range from 150-400% in low rated countries, but (potentially “0%”) with an ADB guarantee

Credit Enhancements

- In the current global economic environment, lenders will continue to require some form of credit enhancements, if they are to finance infrastructure projects in many of the DMCs

What are Credit Enhancements?

- Credit enhancements are a form of risk mitigation
- Offered by MDBs, national governments, and private insurers
- Widely used by lenders and investors in DMCs
- Include guarantees, covering (1) political risks; and (2) comprehensive risks (*i.e.* commercial and political risks); and
- Loan and guarantee syndications

Benefits of Credit Enhancements

- Encourage lenders and investors to finance projects in DMCs they may consider too risky to lend
- Enable lenders to provide longer maturities
- Reduce financing costs

Unique Benefits of an ADB Credit Enhancement

- Lenders take comfort in ADB's due diligence, in particular, to ensure that a project is financially, technically and economically sound, and does not have a negative impact on the environment
- Lenders also take comfort that ADB's participation in a project can resolve potential disputes between a DMC government and the owners of a project quickly

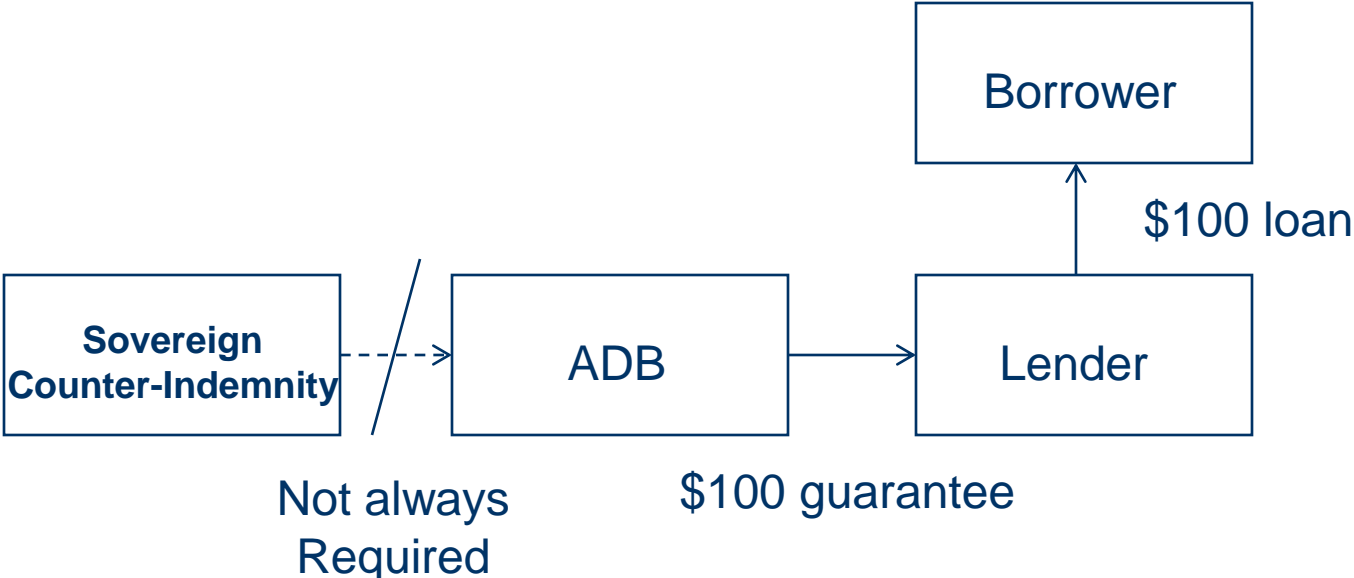
ADB Credit Enhancements

- Guarantees
- Syndications

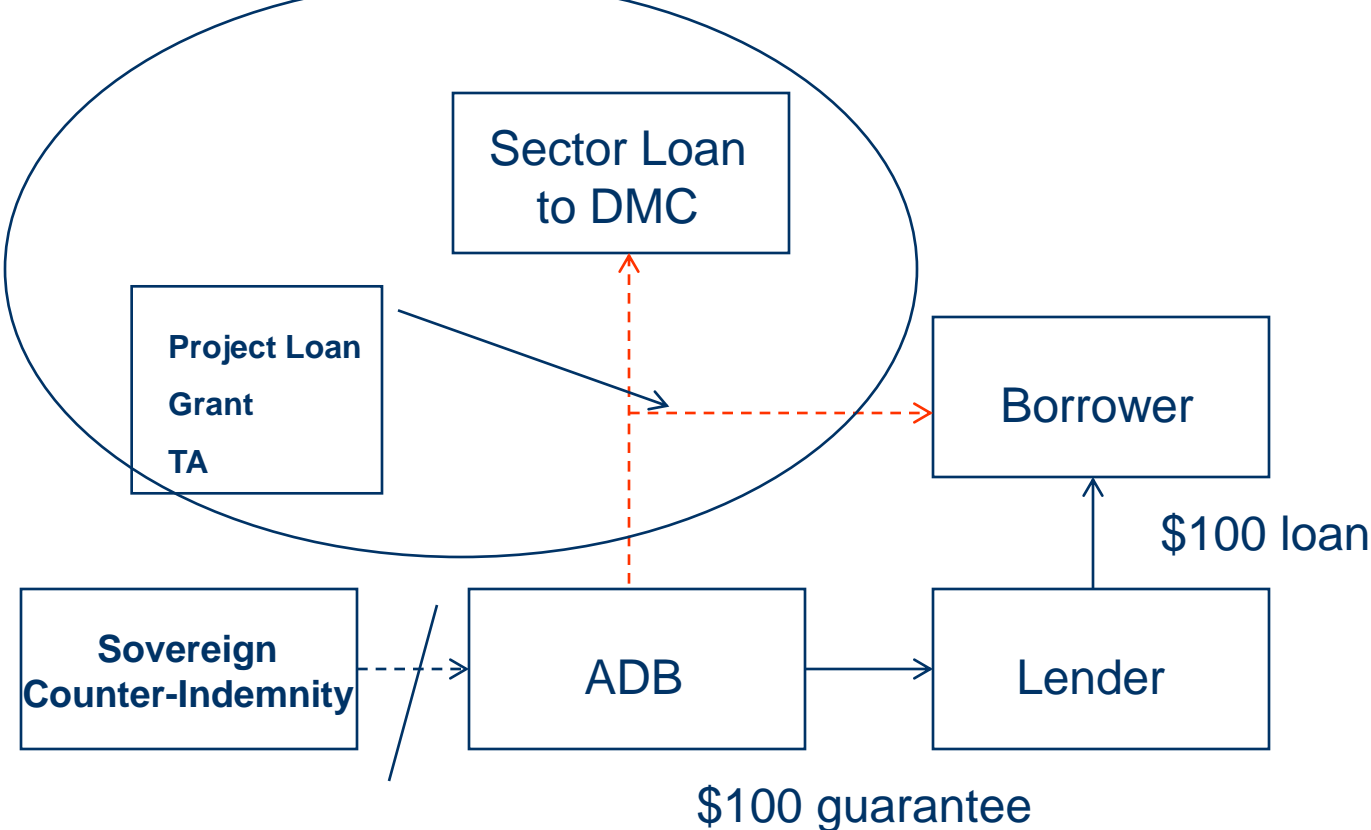
Types of Guarantees

- ADB's Charter does not specify what type of guarantees can be issued
 - Guarantees can cover a wide-range of risks, including:
 - Political risks
 - Comprehensive risks (covering commercial and political risks)

Guarantee Structure



Guarantee – Participation Requirement



Political Risk Guarantee

- Types of risks guaranteed
 - Breach of contract, expropriation, transfer restriction, and political violence (including terrorism), sovereign- non payment
- Various types of loans
 - Bank loans, shareholder loans, loan guarantees
- Up to 100% of principal and interest
- Local currency or foreign exchange loans
- Guarantees issued to local and foreign lenders (investors)
- Long tenors, e.g. 15-20 years

Comprehensive Guarantee

- Covers commercial and political risks
- Only a portion of the debt service guaranteed (e.g. principal only, bullet payment)
- Loans, bonds, securitizations
- Local currency and foreign exchange loans
- Guarantees issued to local and foreign lenders (and investors)
- Long tenors, e.g. 15-20 years

Guarantees Facilitate Financing of Public and Private Sector Projects

- ADB can provide guarantees with or without a sovereign counter-indemnity to ADB
 - Note: Different terms will apply to the guarantee if there is no sovereign counter indemnity (e.g. higher guarantee fees, and lower guarantee amounts)

Pricing for Guarantees

- With sovereign counter-indemnity to ADB
 - 15-20 bps per annum
- No sovereign counter-indemnity to ADB
 - Commercial market prices

Size of an ADB Guarantee

- If a guarantee alone, 40% of the project costs, or \$400 million
- If the guarantee is in combination with other ADB instruments, the lesser of 25% of the project costs or \$250 million (and subject to underwriting)
- Additional amounts of guarantee are available through syndication instruments (reinsurance, guarantee-of-record)
- With sovereign counter-indemnity, amounts of guarantee may be higher

Procurement Guidelines

- Transparent bidding process
- Equipment must be sourced from an ADB member country

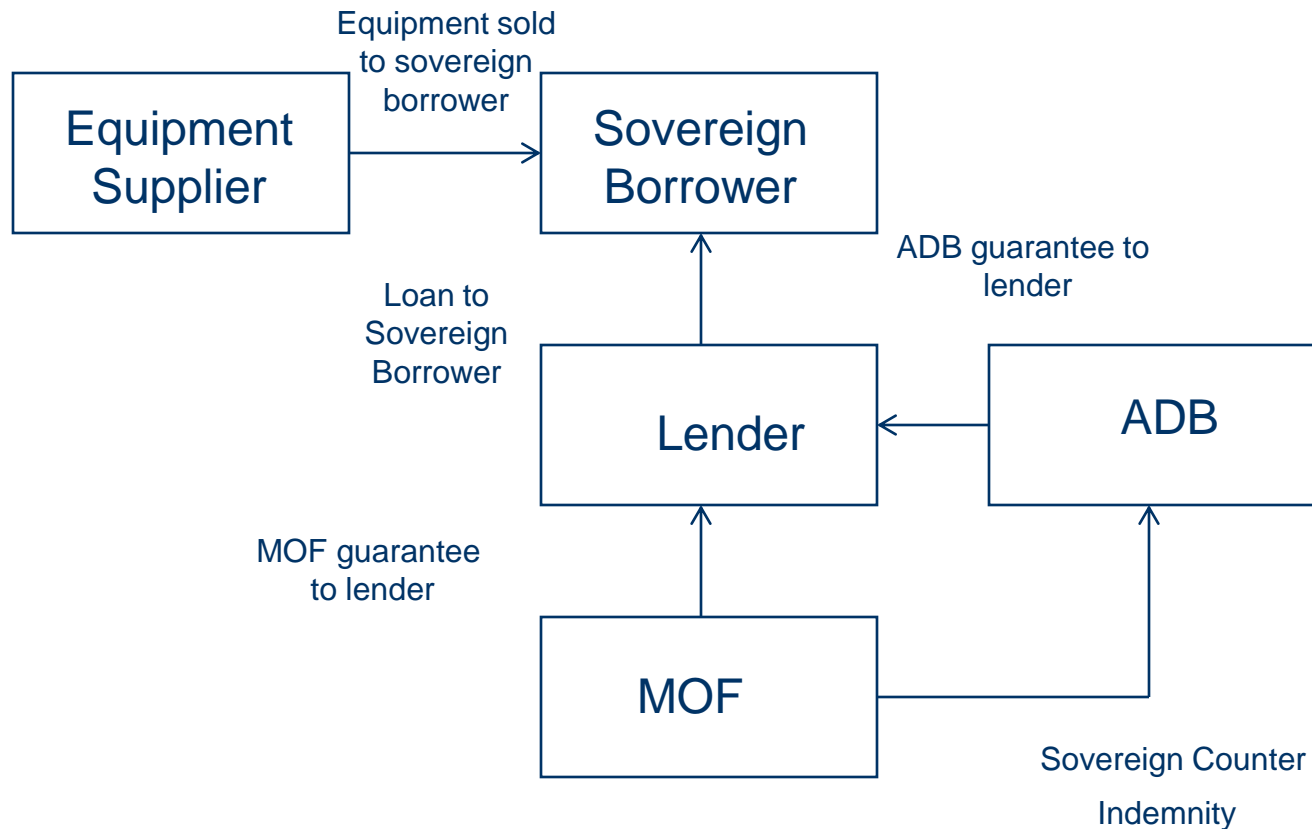
Case Study – Sovereign Non Payment Guarantee - Assumptions

- Government utility requires transmission equipment and financing
- French company prepared to provide equipment
- Commercial bank prepared to provide financing with MOF guarantee and a payment guarantee from ADB
- ADB can provide guarantee with or without sovereign counter-indemnity. With counter-indemnity, fee is 15-20 bps; without counter-indemnity fee is 250 bps

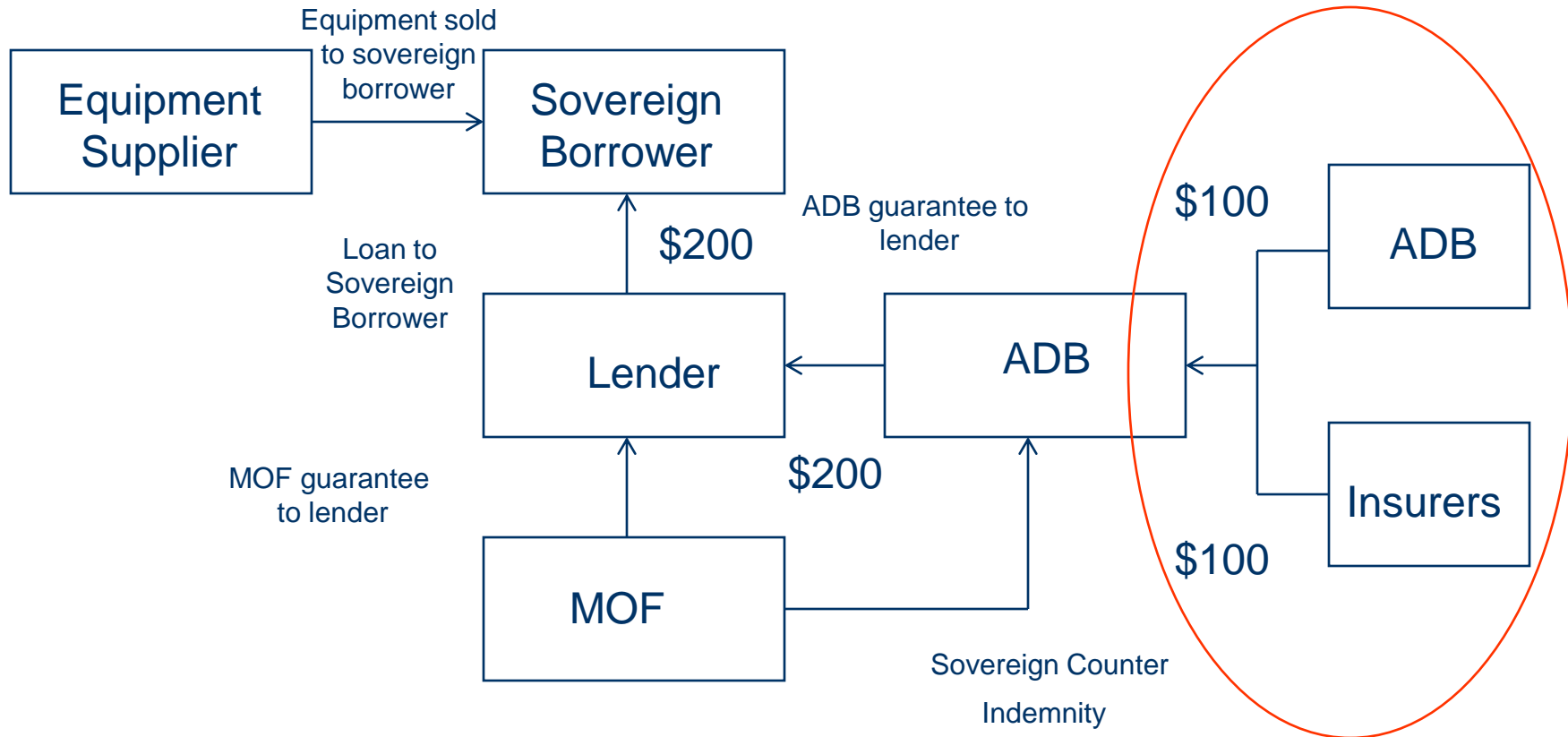
Case Study – Sovereign Non Payment Guarantee - Assumptions

- Amount of guarantee required \$200 million
- ADB can provide only \$100 million guarantee
- ADB can leverage additional \$100 million through various syndication arrangements (e.g. guarantee-of-record)

Case Study – Sovereign Non Payment Guarantee



Case Study – Sovereign Non Payment Guarantee



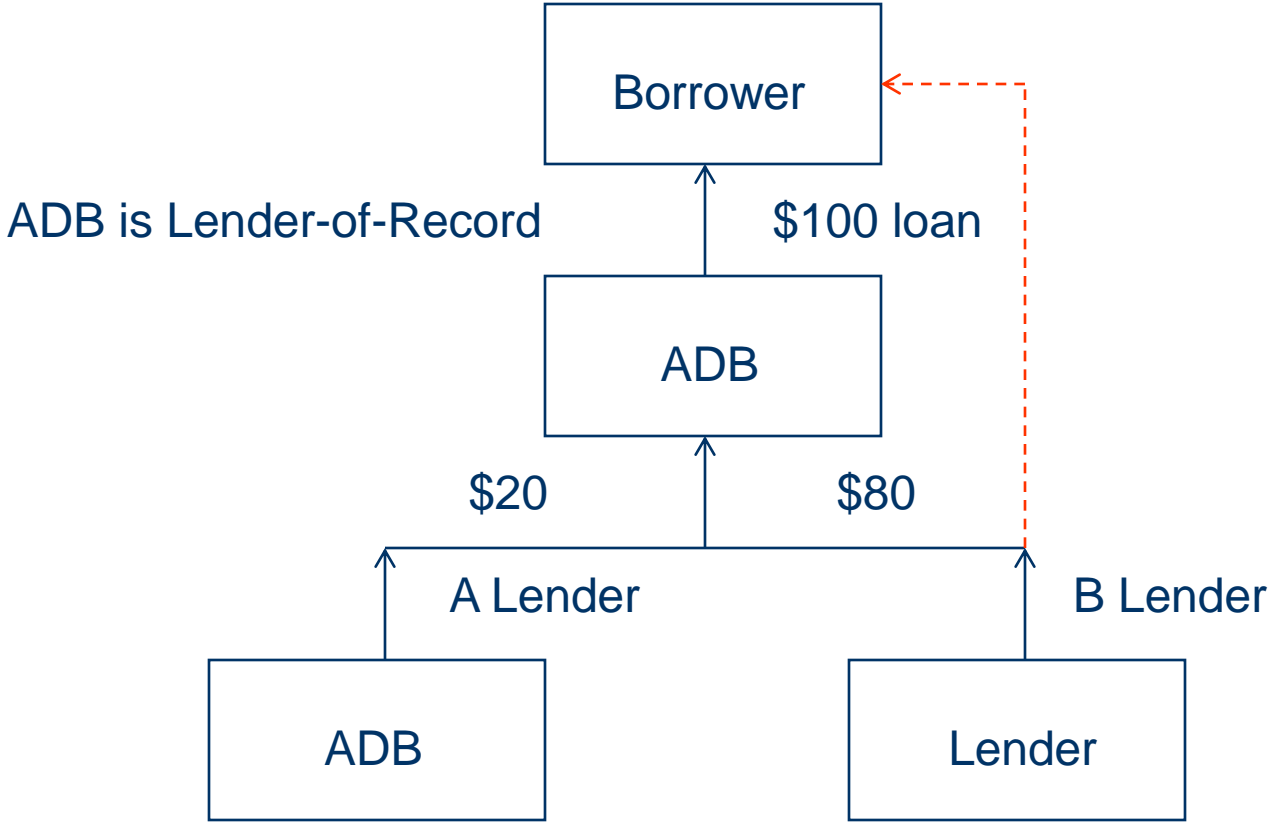
Why Syndications?

- Syndication instruments encourage lenders and political risk insurers to participate in projects that they may not finance or insure on their own given perceived high political risks
- Enables ADB to leverage its own resources and mobilize large amounts of additional capital and insurance
- Banking regulators in many countries recognize that syndication instruments provided by MDBs provide some capital relief from provisioning

Types of Syndication Instruments

- Loan Syndication or “B” loan
- Guarantee-of-record
- Reinsurance
- Unfunded risk participation

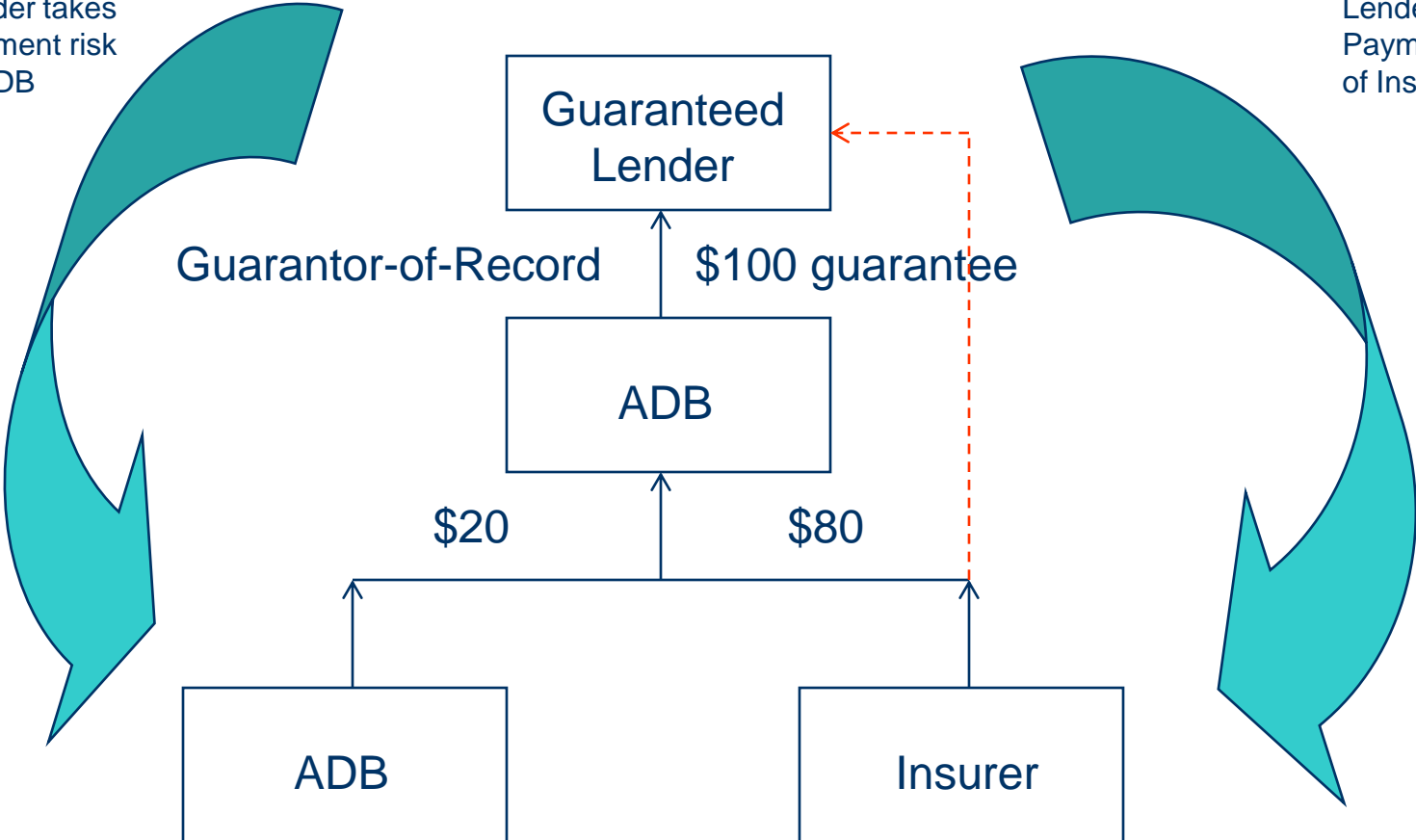
Syndications – B loan



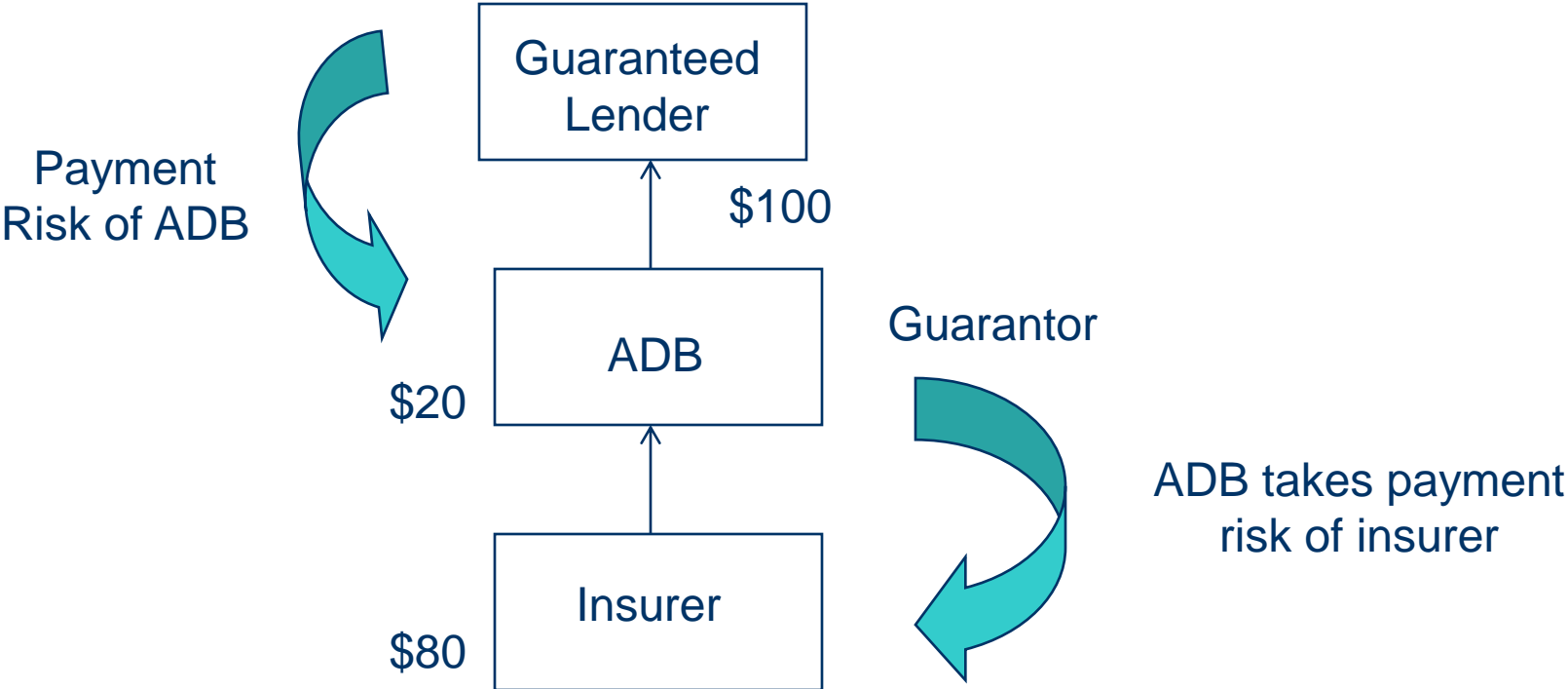
Syndications – Guarantee-of-record

Lender takes
Payment risk
of ADB

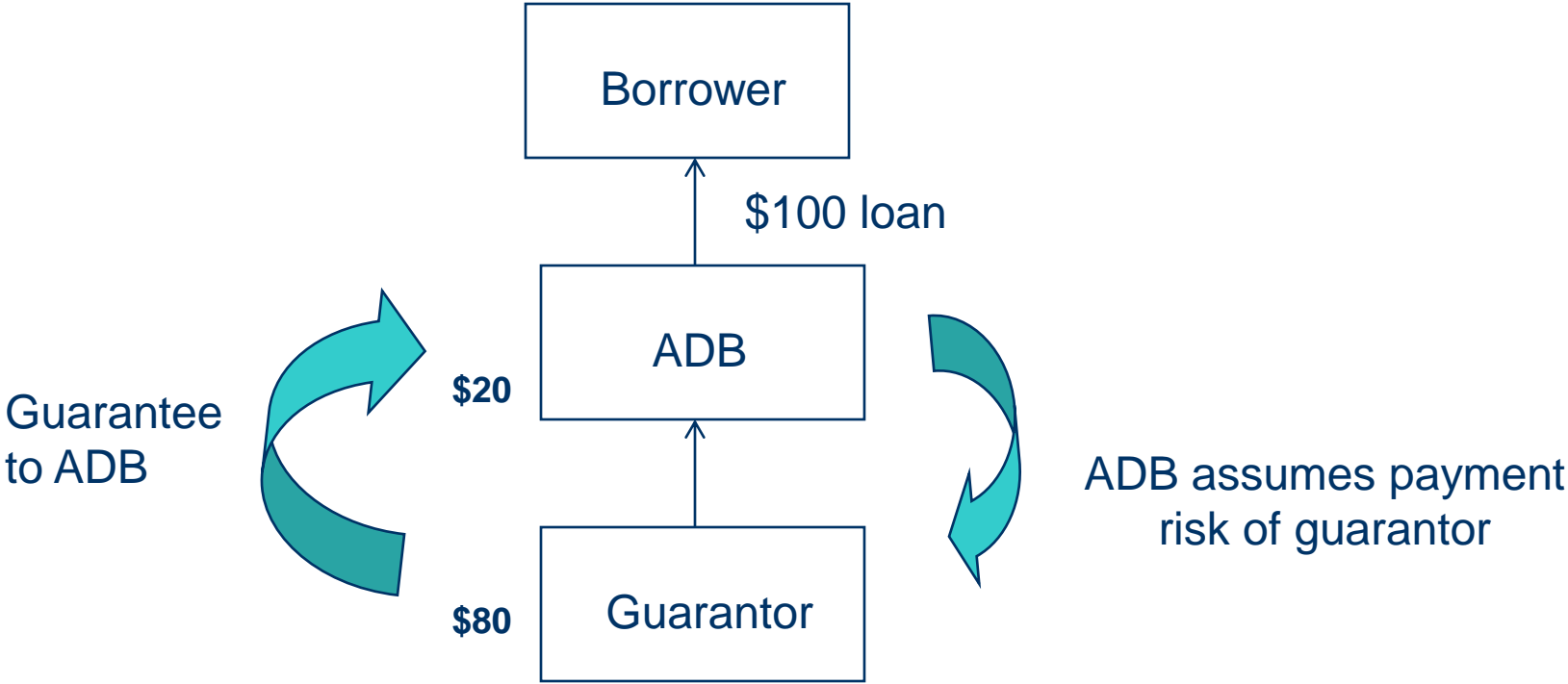
Lender takes
Payment risk
of Insurer



Syndications – Reinsurance



Syndications – Unfunded Risk Participation



Questions?

Thank you

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