PF bankers declare war on The Man

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One thing a hack never wants to do is to give credit to another title for making a fair fist of a story that sits firmly in his/her own sector… but today, this infra scribbler is swallowing pride while doffing a cap to the *FT* for writing a story that impacts infrastructure finance on a global basis.

Credit where credit's due, it has identified an issue that *IJGlobal* has been tracking for some time – one that looks set to impact the global PF community… most pertinently impacting the role that banks play in the sector, leading deals in both project finance and the broader infrastructure finance arena.

This evil is brought to the table by the well-meaning (if misguided) powers-that-be in Europe… mandarins who seek to protect the market from a repeat of the global financial crisis by forcing banks to hold more capital against loans.

And from these finest of intentions, we behold the Basel-led Capital Requirements Directive (CRD IV) which looks set to restrict banks' use of advanced internal rating-based (AIRB) approach to credit risk measurement.

Sadly the European Central Bank – led by folk with minimal experience of infrastructure/project finance – lumps AIRB in with less rigorous financing mechanisms that have been the cause of so much financial woe in recent times.

And so the European Central Bank (ECB) lobs a hand grenade into this peaceable world where the primary focus is to deliver essential infrastructure underpinned by long-tenor debt.

But should we really be that worried? Is this really a death knell for project finance? And haven't people been banging this drum for such a long time that the skin's starting to look a bit loose?

Whatever the case, the banking community's not taking it sitting down.

The fight back

The *FT* article states the case and underlines the threat to the future of long-term lending and the role that the banking community plays in structuring these deals, but it hasn't picked up that lending institutions have already mobilised.

European banks (who have the most to lose) have taken the vanguard to fight against restrictions to their activity and we understand that many of them are currently lobbying the ECB, stating their case against proposed changes and sending strongly-worded letters.

While it remains entirely unclear just how much of an impact CRD IV will have on lending activity in this sector, project finance banks are making their thoughts known and putting forward their "view of life" as one lender puts it.

"There is no final announcement on what the rules are going to be, it is the expectations based on consultations they have held that are leading bankers to take the opportunity to put their case to try to water down capital adequacy requirements," says one active lender.

And the timing's right as this ruling is likely to be brought into force next year (2020), enforced in the next couple that follow to allow banks time to adjust. However, once it's announced, CRD IV will be set in stone – so lobbying needs to ramp up right now.

While it is essential that the industry's opinion be heard, some are concerned about the implications but strongly believe that the market will continue… even if in a different guise.

"I can't see it killing project finance," says another lender. "There have been many declarations of the death of project finance – it just means that the nature of the structures will have to change and pricing will change."

If these changes (whatever they end up being) are pushed through, one thing for certain – it will result in the increased adoption of mini-perm structures, throwing refi risk on to borrowers (which they don't like) and it will not impact all markets… only the ones with established reliance on long tenors. For example, Australia and the US where long-term debt has not gained a significant foothold will shrug with indifference.

The rest of the lending market will have to restructure deals or sell loans on to alternative lenders who seem not to appear on the ECB's radar and those consultants who are not gainfully employed untangling the reference rate debacle will be in demand to help on this front too.

Confused picture

While rattling this fairly impressive sabre at the lending community, Europe does seem to be contradicting itself a little bit as this week it has been bumping its gums about green loans… which it champions.

Therein lies the rub. Green loans are long-tenor and run entirely contrary to the goals of the Capital Requirements Directive.

These ambitions – supporting the delivery of a green economy while creating a safer lending environment – are approaching a fork in the road, with the infra/energy community not knowing which direction it will take… surely, you can't take both paths?

The moral of the tale has to be that to ensure the EBC heads in the right direction (or at the very least to remove the sharpest stones from the path you are forced to take) you'd better be stating your case now... lest you repent at leisure.

Tell me, does it always feel that the lions are commanded by donkeys?